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*Commissioner Ness sworn in on June 3, 1994.
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Before the
Federal Communications Commission
Washington, D.C. 20554

CC Docket No. 90-257

In re Applications of

LA STAR CELLULAR TELEPHONE COMPANY — File No. 27161-CL-P-83

For construction permit for facilities operating on Block B in the Domestic Public Cellular Radio Telecommunications Service in the New Orleans, Louisiana MSA

and

NEW ORLEANS CGSA, INC. — File No. 29010-CL-P-83
File No. 29181-CL-P-85

To amend its construction permit for facilities operating on Block B in the Domestic Public Cellular Radio Telecommunications Service, Call Sign KNK224, in the New Orleans, Louisiana MSA

MEMORANDUM OPINION AND ORDER

Adopted: November 18, 1994; Released: November 28, 1994

By the Commission:

I. INTRODUCTION

1. This memorandum opinion and order reaffirms the dismissal of the application of La Star Cellular Telephone Company (La Star) to construct a cellular telephone system. We find that La Star is ineligible to operate a system on frequency Block B (the wireline block) in this market. We take this action pursuant to a decision by the United States Court of Appeals for the District of Columbia Circuit vacating and remanding for further proceedings our prior decision dismissing La Star's application. *La Star Cellular Telephone Co.*, 7 FCC Rcd 3762 (1992), *vacated and remanded sub nom. Telephone and Data Systems, Inc. v. FCC*, 19 F.3d 655 (D.C. Cir. 1994).

II. COMMISSION DECISION

2. In this proceeding, New Orleans CGSA, Inc. (NOCGSA),[1] which holds a license to operate a cellular telephone system on frequency Block B in the New Orleans MSA, seeks to extend its geographic service area into St. Tammany Parish, Louisiana. La Star Cellular Telephone Company (La Star) filed a mutually exclusive application to operate a cellular system in St. Tammany Parish.

3. The Commission, affirming an initial decision by Administrative Law Judge Joseph Chachkin, dismissed La Star's application as unacceptable for filing. *La Star Cellular Telephone Co.*, 6 FCC Rcd 6860 (I.D. 1991), *aff'd*, 7 FCC Rcd 3762 (1992). The Commission found that La Star is ineligible to file for frequency Block B (the wireline block) because it is not controlled by a wireline carrier with a presence in the cellular market as required by 47 C.F.R. § 22.902(b).

4. La Star is a joint venture owned 51 percent by SJI Cellular, Inc. (SJI) and 49 percent by Star Cellular Telephone Co. (Star). SJI's parent company, SJI, Inc., also owns a telephone company serving a portion of the New Orleans MSA. SJI is therefore eligible to apply for frequency Block B in the New Orleans MSA. By contrast, neither Star's parent company, United States Cellular Company (USCC), nor USCC's parent, Telephone and Data Systems, Inc. (TDS), is eligible to apply in New Orleans. The Commission found that USCC, not SJI, controls La Star, making La Star ineligible.

5. In finding La Star ineligible, the Commission adopted in substance findings by the ALJ concerning the formation of La Star and the prosecution of its application. The Commission found that these circumstances demonstrated the dominant role played by USCC and previously by Maxcell Telecom Plus (Maxcell), USCC's predecessor-in-interest as the 49 percent owner of La Star.

6. These findings (7 FCC Rcd at 3762-64 ¶ ¶ 4-19) indicated that Maxcell took the initiative in the formation of La Star and the preparation and prosecution of La Star's application, including appointing key personnel, acquiring cell sites, and handling financial responsibilities. SJI did not participate with respect to these matters. After the Common Carrier Bureau dismissed La Star's application as untimely, Maxcell, not SJI, was active in successfully appealing this action. *See Maxcell Telecom Plus, Inc. v. FCC*, 815 F.2d 1551 (D.C. Cir. 1987).

7. The findings further indicated that after USCC acquired Maxcell's interest, USCC, like Maxcell, played the dominant role in prosecuting the application. Specifically, the findings disclosed that USCC was principally involved in preparing an October 26, 1987 amendment to La Star's application, in handling La Star's day-to-day affairs and finances, in preparing an application for interim operating authority, and in preparing tax returns. The findings indicated that SJI and USCC did not observe the formalities of the joint venture agreement and that SJI did not significantly involve itself in La Star's affairs until after the Commission designated an issue as to La Star's control.

8. The Commission rejected arguments on behalf of La Star that the above findings did not demonstrate SJI's failure to control La Star. 7 FCC Rcd at 3764-66 ¶ ¶ 24-40. The Commission found that the record concerning

[1] The licensee subsequently changed its name to Louisiana CGSA, Inc. To avoid confusion, we will continue to refer to the licensee as "NOCGSA".

Maxcell's involvement in La Star (which La Star did not dispute) was relevant and probative as to SJI's lack of control. The Commission also found that because La Star did not have an operating facility, evidence concerning the preparation and prosecution of its application was the most probative evidence as to La Star's control.

9. Additionally, the Commission rejected the principal argument on behalf of La Star that USCC's extensive involvement in La Star's affairs, coupled with SJI's lack of involvement, reflected a valid delegation of authority from SJI to USCC. The Commission found that SJI did not establish policy or supervise USCC. Rather, to all appearances, USCC acted on its own.

10. In view of the foregoing, the Commission concluded that SJI did not control La Star and that La Star was therefore not eligible to apply for a wireline authorization.

III. COURT OF APPEALS

11. On March 29, 1994, the United States Court of Appeals for the District of Columbia Circuit vacated and remanded the Commission's decision. The court held that it was unable to determine whether the Commission's analysis was consistent with precedent. First, the court ruled that the Commission did not adequately explain why it did not analyze the facts of this case using the standards set forth in *Intermountain Microwave*, 24 RR 983 (1963).

12. In *Public Notice*, 1 FCC Rcd 3 (1986), the Commission stated that the *Intermountain* criteria would be used to evaluate the control of applicants for cellular authorizations. The six *Intermountain* factors are as follows:

(1) Does the licensee have unfettered use of all facilities and equipment?

(2) Who controls daily operations?

(3) Who determines and carries out the policy decisions, including preparing and filing applications with the Commission?

(4) Who is in charge of employment, supervision, and dismissal of personnel?

(5) Who is in charge of the payment of financing obligations, including expenses arising out of operating?; and

(6) Who receives moneys and profits from the operation of the facilities?

13. The *Intermountain* factors represent the normal incidents of responsibility for the operation and control of a common carrier facility. 24 RR at 984. As such, they generally provide useful guidelines for evaluating real-party-in-interest and transfer of control questions. For example, in the *Public Notice* cited above, the Commission explicitly adopted the *Intermountain* criteria as guidelines for questions arising from the use by cellular operators of management companies. We stress, however, that there is no exact formula for determining control and that questions of control turn on the specific circumstances of the case. *See Data Transmission Co.*, 44 FCC 2d 935, 936 (1974). Thus, in applying the *Intermountain* criteria, we examine the totality of the circumstances.

14. Second, the court found that the Commission's analysis of the control issue in this case was inconsistent with that in *Ellis Thompson Corp.*, 7 FCC Rcd 3932 (1992), which the Commission decided contemporaneously.[2]

15. Following remand the parties were invited to comment on what further action should be taken. *La Star Cellular Telephone Co.*, FCC 94I-040 (Apr. 20, 1994).[3]

IV. ISSUE ANALYSIS

A. APPLICABILITY AND RELEVANCE OF INTERMOUNTAIN

16. *Comments.* The parties uniformly urge that the *Intermountain* criteria should be considered in this case. They argue, however, that the criteria are merely guidelines and not a precise formula. Thus, the commenters assert that the guidelines should be applied flexibly based on the particular facts of this case. La Star contends that the criteria should be applied in light of precedent that participation by a minority owner in the licensee's affairs does not support an inference of control. NOCGSA and PCC[4] suggest that some of the *Intermountain* criteria may not be applicable in this case because La Star has no operating facility. NOCGSA and the Bureau submit that the control test must be applied as of the time the application was filed and at all times thereafter.

17. *Discussion.* Pursuant to the court's directive, we will apply *Intermountain* to this case. We note, however, that this case presents a special problem in applying the *Intermountain* criteria, since the issue here involves the interests in the applicant for purposes of threshold eligibility to file an application rather than control of an operating facility. *See Cellular Communications Systems*, 93 FCC 2d 683, 692 ¶.¶ 24-25 (1983). Accordingly, we have no record of actual conduct with respect to several aspects of

[2] The court reversed and remanded the Commission's *Ellis Thompson* order for futher consideration. *Telephone and Data Systems, Inc. v. FCC*, 19 F.3d 42 (D.C. Cir. 1994). We have today adopted a further order in the *Ellis Thompson* proceeding. *Ellis Thompson Corp.*, FCC 94-( ).

[3] Before the Commission are: (1) comments, filed May 5, 1994, by La Star, NOCGSA, TDS, and the Common Carrier Bureau, and PCC Management Corporation (PCC); and (2) reply comments, filed May 12, 1994, by American Cellular Network Corporation (Amcell), La Star, and NOCGSA, and May 17, 1994, by TDS and the Bureau. Amcell is a party to the *Ellis Thompson* proceeding, in which comments on the interrelation of the issues in the two cases were invited. *Ellis Thompson Corp.*, 9 FCC Rcd 1888 (G.C. 1994). PCC is not a party to this proceeding or to *Ellis Thompson*. We will accept its comments as an *amicus*.

[4] PCC proposes that the Commission should update the applicability of the *Intermountain* criteria and approve "safe harbor" provisions for agreements between cellular licensees and management companies. Without here considering whether a general policy review in this area is warranted, none of PCC's specific proposals would justify a different outcome in this proceeding. In particular, we cannot, on the record of this case, rely on the parties' formal agreements alone, as PCC proposes in some situations, to make a meaningful assessment of *de facto* control. Nor would the adoption of PCC's suggested safe harbor provisions change the analysis here. Moreover, to the extent that the parties and PCC have called to our attention information about the current realities of cellular telephony, we have incorporated that information in our analysis.

the *Intermountain* factors that would indicates who could be expected to exercise control over the system in the future.

18. We find that, in this regard, the applicant's representations as to its intentions, and related contractual provisions, are relevant. *See News International, PLC*, 97 FCC 2d 349, 356 ¶ 17 (1983). The probative value of these representations and provisions must, however, be evaluated in light of the record as a whole. Where the applicant's actual conduct has been shown to be inconsistent with its representations and agreements, crediting them would not be warranted.

19. With this in mind, we turn to our evaluation of the *Intermountain* factors. In this regard, the court's opinion did not question the factual findings on which our previous conclusions rested. Although, as TDS points out, the court vacated our decision, and thereby rendered it without effect, the court did not in any way disapprove our specific factual findings. Thus, we believe that the court gave us the discretion to reaffirm our previous findings if we continue to believe that they are supported by the record. *See* 47 U.S.C. § 402(h). We find no reason to depart from our previous findings, and we reaffirm them.[5]

B. THE INTERMOUNTAIN FACTORS

1. Use of the Facilities

20. *Comments.* La Star and TDS observe that the applicant has no operating facilities at this time. They submit that, under terms of La Star's joint venture agreement, all facilities will be owned by La Star and operated under the control of SJI with SJI's president, John Brady, serving as general manager. NOCGSA responds that, in the absence of operating facilities, this factor is irrelevant to the present case. The Bureau maintains that La Star's representations and agreement should not be credited because other aspects of this record indicate that La Star has not acted consistently with the provisions of the joint venture agreement and cannot be expected to do so in the future.

21. *Discussion.* As indicated above, we consider La Star's representations and contractual provisions regarding its facilities as relevant to this case. Thus, the sole evidence as to this factor indicates that SJI will have unfettered use of all facilities and equipment. However, the weight to be given this evidence can only be determined after all circumstances bearing on its probative value have been examined. We will address this matter in our overall summary of the factors.

2. Day-to-Day Operations

22. *Comments.* As under the previous factor, La Star and TDS point out that there are no operating facilities and therefore no record of existing day-to-day operations. They reiterate that, under the joint venture agreement, day-to-day operations will be supervised by SJI, with Brady as general manager. NOCGSA and the Bureau reply that, although there is no record of any operating facility, the record reflects La Star's day-to-day activities in the preparation and prosecution of its application. They note that the Commission found that Maxcell and then USCC, rather than SJI, dominated these activities.

23. *Discussion.* We find that the sole evidence under this factor consists of representations that SJI will exercise control through its supervision of the day-to-day operations of the cellular telephone system. The weight to be given this evidence will be discussed in our overall summary.

3. Policy Decisions

24. *Comments.* La Star and TDS once again do not dispute the finding that during the period that Maxcell was La Star's minority owner, Maxcell, rather than SJI, dominated the preparation and prosecution of La Star's application. They reiterate the argument, previously rejected by the Commission, that USCC's extensive involvement in La Star's application reflected legitimate participation by a minority owner and not an inappropriate exercise of control.

25. NOCGSA and the Bureau contend that the record amply demonstrates that USCC, as well as Maxcell, dominated La Star's affairs in this regard.

26. *Discussion.* The record provides abundant evidence of the parties' actual conduct in the determination and carrying out of policy decisions in relation to the preparation and prosecution of La Star's application. As noted in our prior decision, the parties do not seriously challenge the finding that Maxcell controlled such matters during the period that Maxcell held a minority interest in La Star. 7 FCC Rcd at 3764-65 ¶ ¶ 25, 30. (A finding that Maxcell controlled La Star itself renders La Star ineligible, since an applicant must be eligible from the time its application is filed. *See Cellular Communications Systems, supra.*)

27. As to the period in which USCC held a minority interest in La Star, we specifically considered and rejected the contention that USCC's extensive participation in determining La Star's policies as reflected in the prosecution of its application was pursuant to a valid delegation of authority from SJI. We found that (with one exception) the record reflected no meetings of La Star's management committee or other evidence that policy decisions were made in accordance with the provisions of La Star's joint venture agreement, which provided for control by SJI. 7 FCC Rcd at 3765 ¶ 31. We also found no support for the contention that SJI had issued policy directives through La Star's attorney Arthur Belendiuk. We found that Belendiuk had been associated with Maxcell and not SJI, and that SJI had used other counsel in matters unrelated to this proceeding. *Id.* at 3765 ¶ ¶ 32-33. While the record demonstrated extensive input by USCC and its personnel in matters

[5] We find no merit to questions as to our findings raised by TDS and La Star. For example, TDS charges that the Commission erroneously found that USCC prepared a 1987 amendment to La Star's application, a 1987 pleading, and a 1988 application for interim operating authority. TDS asserts that these matters were prepared by La Star's attorney, Arthur Belendiuk, and executed by John Brady, the president of SJI. The Commission's point, however, was that USCC had done the significant substantive work on these matters without any participation by SJI, a finding which TDS's allegations do not disturb. 7 FCC Rcd at 3763 ¶ ¶ 15-16, 3765-66 ¶ ¶ 33-36. La Star challenges the Commission's finding that no general manager of La Star was appointed, as provided by La Star's joint venture agreement. While La Star observes that it represented to the Commission that Brady would be La Star's general manager, it points to no evidence that, pursuant to the joint venture agreement, the management committee made a formal appointment. Brady himself testified that the formalities of the agreement were not enforced. Tr. 1078-79.

handled by Belendiuk, the little involvement that SJI claimed proved to be insubstantial and lacking in credibility. *Id.* at 3765 ¶ ¶ 34-36. We found that, to all appearances, Belendiuk acted as USCC's counsel and USCC supervised the prosecution of the application. As noted above, we find no reason to revisit these findings, which strongly support a conclusion that USCC effectively determined and carried out policy and controlled La Star.

4. Personnel Responsibilities

28. *Comments.* Consistent with their other claims regarding La Star's future operations, La Star and TDS assert that SJI, will supervise personnel matters, such as hiring and firing. They deny that USCC has hired any of La Star's key personnel. NOCGSA and the Bureau answer that SJI did not hire the key personnel associated with prosecuting La Star's application. Rather, they assert that the key hiring decisions were made by Maxcell.

29. *Discussion.* The claim that SJI will be in charge of personnel matters in La Star's future operations is contradicted by the parties' actual conduct to this point. Maxcell hired La Star's attorneys, economic consultants, and a local real estate agent. 7 FCC Rcd at 3763 ¶ ¶ 8-9. By contrast, in matters unrelated to this proceeding, SJI did not use any of these individuals. *Id.* at 3763 ¶ 11. Other work on the La Star application was done directly by Maxcell or USCC personnel. *Id.* at 3763-64 ¶ ¶ 8, 15-17. We find that this evidence undermines the claim that SJI will be in charge of personnel matters in La Star's proposed operation.

5. Financial Obligations

30. *Comments.* La Star and TDS claim that pursuant to their joint venture agreement, SJI and USCC will pay pro rata shares of all expenses. They assert that USCC has never attempted to exert financial leverage against SJI. NOCGSA and the Bureau contend that SJI and USCC did not previously treat their financial obligations on a pro rata basis or in accordance with the joint venture agreement.

31. *Discussion.* The record discloses SJI's failure to be in charge of financial obligations in the preparation and prosecution of La Star's application. Maxcell's principal obtained the bank commitment used to finance La Star's proposal. 7 FCC Rcd at 3763 ¶ 8. The bank involved had previous associations with Maxcell but not with SJI. Until the Commission designated a control issue, the joint venture agreement provided that Maxcell and then USCC would pay all expenses for the prosecution of the application and that SJI would not be liable until after grant of a construction permit. *Id.* at 3763 ¶ 8, 3766 ¶ 37. Accordingly, USCC personnel handled all aspects of La Star's finances, including paying expenses, recordkeeping, and handling tax returns. *Id.* at 3763-64 ¶ ¶ 15-18, 3766 ¶ 37. SJI received no documentation of La Star's expenses. To some degree USCC commingled La Star's business and its own. *Id.* at 3766 ¶ 38. We find that this evidence undermines the claim that SJI has been or will be in charge of the payment of financing obligations to the degree indicated by the joint venture agreement.

6. Receipt of Monies and Profits

32. *Comments.* La Star and TDS claim that pursuant to their joint venture agreement, SJI will oversee billing and receipts and that it and USCC will receive a pro rata share of all profits. NOCGSA and the Bureau object that La Star did not previously conduct its financial affairs on a pro rata basis consistently with the joint venture agreement. In this regard, they submit that, because USCC was solely liable for financing the prosecution of the application, it has first claim against the profits of the proposed operation.

33. *Discussion.* We find that La Star's failure to conduct its finances on a pro rata basis and in accordance with its joint venture agreement diminishes the credibility of its claim that SJI will receive profits and monies on that basis in the future.

C. OVERALL SUMMARY

34. We find that the record, when analyzed in light of the *Intermountain* criteria, continues to provide strong support for our conclusion that SJI, the wireline-eligible entity, does not control La Star and that La Star is therefore ineligible for this authorization. Because La Star does not have an operating facility, we do not have a record of actual conduct with respect to all of the *Intermountain* factors. However, the record of actual conduct relevant to factors 3-5 consistently reflects the domination of La Star's affairs, first by Maxcell and then by USCC, and the corresponding lack of involvement by SJI. We find that this evidence provides the most probative basis on which to reach conclusions as to the past and likely future control of La Star. *See also* 7 FCC Rcd at 3764-65 ¶ ¶ 26-29. We thus conclude that it outweighs the contractual provisions and representations favoring the appropriate retention of control relied on by La Star under factors 1, 2, and 6. In sum, based on the record, we conclude that SJI does not control La Star and that its application was properly dismissed because La Star is not an eligible wireline applicant.

V. ORDERS

35. ACCORDINGLY, IT IS ORDERED, That the application of La Star Cellular Telephone Company (File No. 27161-CL-P-83) IS DISMISSED with prejudice; and that the applications of New Orleans CGSA, Inc. (File Nos. 29010-CL-P-83, 29181-CL-P-85) ARE GRANTED.

36. IT IS FURTHER ORDERED, That this proceeding IS TERMINATED.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

Before the
Federal Communications Commission
Washington, D.C. 20554

LETTER
January 31, 1994

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In re: KRTH(FM), Los Angeles, CA
Assignment of License
BALH-930618GE

Dear Counsel and Mr. Wildmon:

This is in reference to the above-captioned application for consent to assign the license for KRTH(FM), Los Angeles, California, from Beasley FM Acquisition Corp. ("Beasley") to Infinity Broadcasting Corp. of California ("Infinity"). On August 5, 1993, Americans for Responsible Television ("ART") filed a pleading styled as a "petition to deny" the assignment application.[1] Informal objections were filed on July 14, 1993 and November 24, 1993 by Diane Vudmaska and the American Family Association ("AFA"), respectively.[2]

As an initial matter, the informal objection filed by Ms. Vudmaska consists of a copy of a civil lawsuit alleging that the termination of her employment at the station without good cause resulted in a breach of contract and a breach of covenant of good faith and fair dealing. This action, filed in the Superior Court, County of Los Angeles, California is entitled *Diane Vudmaska v. Beasley FM Acquisition, dba KRTH, a division of Beasley FM Acquisition*. The Commission has consistently held that it is not the proper forum for resolving such private disputes, and that redress should properly be sought in local courts of competent jurisdiction. *John R. Runner, Receiver (KBIF)*, 36 RR 2d 773, 778 (1976); *Decatur Telecasting, Inc.*, 7 FCC Rcd 8622, 8624 (1992); *Listener's Guild, Inc. v. FCC*, 813 F. 2d 465, 469, 62 RR 2d 866, 870 (D.C. Cir. 1987). Accordingly, we will deny Ms. Vudmaska's objection.

With respect to the ART "petition to deny," we note that ART failed to supply an affidavit of any person with personal knowledge attesting to ART's claim to be a party in interest or to the facts alleged in the pleading. Accordingly, the ART pleading does not meet the procedural requirements for a petition to deny imposed by Section 309(d)(1) of the Communications Act of 1934, as amended, 47 U.S.C. § 309(d)(1). Nevertheless, we will treat ART's "petition" as an informal objection pursuant to Section 73.3587 of the Commission's rules.

In its informal objection, ART argues that the Commission should deny the above-referenced application on two grounds. First, ART avers that Infinity's "pattern of repeated violations ofCommission indecency standards" make Infinity an unfit licensee.[3] Second, ART states that Infinity-controlled stations continued to broadcast indecent material in violation of the indecency statute, 18 U.S.C. Section 1464, even after the Commission issued a December 18, 1992 Notice of Apparent Liability (NAL), *Infinity Broadcasting Corporation*, 8 FCC Rcd 2688 (1992), to Infinity for apparent violation of the indecency standard.

To support its first argument, ART provides copies of Commission NAL's previously issued against Infinity for indecency violations. ART states that the NAL issued on December 18, 1992 proposed a forfeiture amount of $600,000, the highest amount ever proposed by the Commission. ART argues that, since the courts have upheld the Commission's authority to enforce the indecency proscription,[4] the Commission's previous determinations demonstrate that grant of the instant assignment application would not be in the public interest.

In support of its second argument, ART includes transcripts of the January 4 through January 13, 1993 and June 4, 1993 broadcasts of the Howard Stern Show by Infinity-controlled stations. These transcripts were contained in complaints dated March 10, 1993 and June 7, 1993 which were filed with the Commission by Mr. Al Westcott. ART

[1] Infinity and Beasley filed separate oppositions on August 16, 1993, and ART filed a consolidated reply on August 23, 1993.
[2] Beasley responded to Ms. Vudmaska's informal objection on September 30, 1993.
[3] The informal objection filed by AFA raises the same argument. Accordingly, we will address the argument as it was presented by ART.
[4] ART cites *FCC v. Pacifica Foundation*, 438 U.S. 726 (1978); *Action for Children's Television v. FCC*, 852 F. 2d 1332 (D.C. Cir 1988).

argues that these transcripts demonstrate that Infinity-controlled stations continue to violate the indecency standard. ART also cites language from the December 18, 1992 NAL issued to Infinity stating that any future failure on the part of Infinity or its subsidiaries to comply with the indecency proscription will result in further appropriate enforcement actions. ART argues that denial of the instant application is such an appropriate action because the transcripts contained in its informal objection demonstrate that Infinity has continued to violate 18 U.S.C. Section 1464. ART's informal objection concludes that Infinity has not attempted to comply with the law and posits that Infinity views indecency fines merely as a cost of doing business.

Infinity's opposition states that the "petition" has no merit, that ART has distorted Infinity's record as a licensee and that the Commission's recent grant of assignment applications to Infinity show that the Commission has determined that it is fit to be a licensee. Further, Infinity argues that Section 504(c) of the Communications Act precludes the Commission from considering pending NAL's in this proceeding.[5]

In support of its contention that ART's informal objection is without merit, Infinity contends that ART has distorted its record of compliance with the Commission's rules. Rather than the "substantial record of FCC violations and fines" that the informal objection attributes to Infinity, the proposed assignee argues that in its twenty year history as a broadcast licensee it has had only one forfeiture actually levied against it, for $6,000 with respect to a December 1988 broadcast. Infinity states that action is not yet final because, on June 21, 1993, it filed a petition for reconsideration of an earlier denial of a petition for reconsideration, *Sagittarius Broadcasting Corp.*, 8 FCC Rcd 3600 (1993).[6] Infinity further faults ART for ignoring what Infinity considers to be its exemplary record of contributions to the communities served by its stations. In support of this contention, Infinity provides numerous letters written by charitable and community organizations in appreciation of various efforts of Infinity-controlled stations on their behalf.

Next, Infinity argues that the Commission's grant of recent assignment of license applications to Infinity[7] is evidence that the Commission has determined that Infinity is fully qualified to be a licensee. Moreover, Infinity cites the Commission's August 12, 1993 NAL,[8] issued to Infinity for apparent indecency violations during broadcasts aired in November and December 1992 and January 1993, stating that, "our records reflect that no other actionable indecency complaints have been filed against Infinity or the Howard Stern Show' [as of the date of the NAL]," as evidence that material included in the informal objection has been found by the Commission to be not actionably indecent. Finally, Infinity argues that Section 504(c) of the Communications Act precludes the Commission from considering pending NAL's or a non-final forfeiture order based on an NAL to Infinity's detriment in this proceeding.[9]

Beasley's opposition offers three arguments for the Commission to deny the informal objection and grant the assignment application. First, Beasley asserts that the instant proceeding is not the appropriate forum for adjudicating indecency complaints involving broadcasts by other stations owned by Infinity. Second, Beasley states that denial of this application would unfairly penalize Beasley for activities of Infinity stations which are unrelated to station KRTH(FM). Finally, Beasley argues that the issues raised in the informal objection are moot because the Commission's August 12, 1993 NAL issued to Infinity states that the monetary forfeiture therein being imposed on four Infinity stations would "adequately address the apparent indecency violations resulting from the broadcasts" considered by the Commission.

In its consolidated reply, ART denies that its informal objection distorted Infinity's record of compliance with Commission rules and states that differing methods of defining and computing previous violations can result in differing totals to describe the number of previous violations. Additionally, ART states that it did not ignore positive aspects of Infinity's record of compliance and of service to the community; rather it contends that such considerations may be appropriately considered if and when the application is designated for hearing, but are premature at this stage of the proceeding.

ART also contends that Section 504(c) of the Communications Act serves only to prevent the use of an unpaid NAL as *prima facie* evidence against a licensee, but that it does not bar a hearing under Section 309(e) of the Act if a substantial and material question of fact has been raised as to whether grant of this assignment application would serve the public interest, convenience and necessity. ART asserts that its informal objection has raised such substantial and material questions of fact. Further, ART states that

[5] Additionally, in its opposition, Infinity claims that ART engaged in a prohibited *ex parte* communication with decision making personnel during a restricted proceeding, in violation of Section 1.1208 of the Commission's rules. To support that claim, Infinity provides the Declaration of Elaine R. Baker stating that on August 6, 1993 (the day after the "petition" was filed) she attended a Michigan Association of Broadcasters reception and "roast" for Commission Chairman James Quello at which she heard Ms. Terry Rakolta (Director of ART) say to Chairman Quello, "K-Earth," and immediately thereafter, "How can you let them buy it?" Ms. Baker states that she did not hear any response from Chairman Quello to Ms. Rakolta's statement. ART's reply provides an affidavit from Ms. Rakolta unequivocally denying Ms. Baker's assertion on this matter, and averring that Ms. Baker was mistaken in what she thought she heard. In light of this denial and the hearsay character of the allegations, we find the evidence insufficient to raise a substantial and material question as to whether ART violated the Commission's *ex parte* rule, 47 C.F.R. Section 1.1208.

[6] The latter petition for reconsideration has since been denied by the Commission. *Sagittarius Broadcasting Corp.*, 8 FCC Rcd 7975 (1993).

[7] Infinity cites to 8 FCC Rcd 2714 (1992) (granting assignment of license applications to Infinity for stations WZGC(FM), Atlanta, GA, WUSN(FM), Chicago, IL and WZLX(FM), Boston, MA), as well as to the August 12, 1993 grant of assignment of license of station WIP(AM), Philadelphia, PA, to Infinity.

[8] *Infinity Broadcasting Corporation*, 8 FCC Rcd 6740 (1993).

[9] Section 504(c) states:

In any case where the Commission issues a notice of apparent liability looking toward the imposition of a forfeiture under this Act, that fact shall not be used, in any other proceeding before the Commission, to the prejudice of the person to whom such notice was issued, unless (i) the forfeiture has been paid, or (ii) a court of competent jurisdiction has ordered payment of such forfeiture, and such order has become final.

Beasley's argument that it would be unfairly penalized by denial of this application is without merit. In support of this assertion, ART argues that the subject application is distinguishable from the recently approved assignment of three radio stations from Cook Inlet Radio License Partnership, L.P. to Infinity, in which the Commission articulated a desire to not penalize the innocent assignor.[10] ART asserts that the earlier assignments are distinguishable because Infinity had stated that it would not broadcast the Howard Stern Show on the stations it obtained from Cook Inlet. Finally, ART argues that the issues raised in its informal objection have not been rendered moot by either the August 12, 1993 NAL issued to Infinity or the grant of the assignment of license of station WIP(AM) to Infinity.

We will deny AFA's and ART's objections. First, the Commission has fully considered the pattern of apparent misconduct cited in its December 1992 NAL issued to Infinity and determined that the subject conduct did not disqualify Infinity as a licensee. Specifically, on December 18, 1992, the Commission approved the assignment of licenses of stations WZGC(FM), Atlanta, Georgia; WUSN(FM), Chicago, Illinois; and WZLX(FM), Boston, Massachusetts, to Infinity. In taking this action, the Commission determined that Infinity was qualified to hold broadcast licenses notwithstanding the apparent misconduct which the Commission had concurrently noted in the December 1992 NAL. *See Cook Inlet Radio License Partnership, L.P.*, 8 FCC Rcd 2714 (1992). Accordingly, the objectors' contention that the apparent pattern of Infinity misconduct reflected in the December 1992 NAL raises a substantial and material question of fact concerning Infinity's basic qualifications is moot.

We also find moot ART's contention that certain conduct by Infinity subsequent to the apparent violations detailed in the December 1992 NAL demonstrates a continued and disqualifying disregard for Commission rules. Specifically, the Howard Stern broadcast on January 13, 1993, upon which ART partly relies, was fully addressed by the Commission in an NAL issued to Infinity on August 12, 1993. Therein the Commission carefully evaluated the nature and extent of the programming at issue as well as relevant mitigating circumstances and concluded that "a monetary forfeiture will adequately address the apparent indecency violations resulting from the broadcasts. . . ." *Infinity Broadcasting Corporation*, 8 FCC Rcd 6740, 6741 (1993). Moreover, based on this determination, the staff, on August 12, 1993, approved the assignment of license of WIP(AM), Philadelphia, Pennsylvania, to Infinity.[11] With respect to the June 4, 1993 Howard Stern broadcast, which was the subject of an indecency complaint filed by Mr. Al Westcott, the staff has dismissed the complaint on the grounds that the material involved was not actionably indecent.[12]

The Commission is aware of six further indecency complaints filed against material aired during the Howard Stern show as broadcast by either Infinity-owned stations or by stations carrying the Howard Stern show by contractual arrangement with Infinity.[13] We have carefully reviewed these complaints and determined that the material cited in them is, for the most part, not actionably indecent under existing Commission criteria. We are today issuing a Notice of Apparent Liability to Infinity in the aggregate amount of $400,000 with respect to the remaining material that we have concluded does fall within our definition of indecent broadcast programming.[14] We are aware that we have previously indicated that Infinity's continuing course of apparent misconduct in this area is troubling and that further violations might provoke more stringent penalties than monetary forfeitures. *See, e.g., Infinity Broadcasting Corporation*, 8 FCC Rcd 6740, 6741 (1993). We conclude, however, that such action is not warranted at this time. Recently, the Court of Appeals for the District of Columbia Circuit in *Action For Children's Television v. FCC*, Case No. 93-1092 (D.C. Cir. Nov. 23, 1993) (*ACT III*) directed the Commission to conduct further proceedings as to various aspects of our indecency enforcement program. Although we do not read the Court's decision to restrict our ability to enforce against broadcast indecency, except with regard to the Midnight to 6:00 a.m. safe-harbor period, we recognize that the opinion has raised issues regarding our enforcement program that can most appropriately be ad-

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[10] *Cook Inlet Radio License Partnership, L.P.*, 8 FCC Rcd 2714 (1992).

[11] ART contends that its petition is not mooted by the Commission's prior decisions involving Infinity because "NALs under § 503 and administrative sanctions under § 312 are different and independent enforcement mechanisms available to the Commission, as is the Commission's authority to hold hearings and make findings under § 309." Whatever the merit of this asserted distinction, the decisions noted above approving the sale of Cook Inlet's stations and the sale of WIP(AM) to Infinity reflect express determinations under § 309 that the assignments of licenses sought in the underlying applications raised no substantial and material question of fact and that grant of the applications would serve the public interest, convenience and necessity. *See* 47 U.S.C. §§ 308, 309 and 310.

[12] *See Letter to Al Westcott* (September 13, 1993).

[13] Five of these complaints, as detailed below, were filed by Mr. Al Westcott:

Complaint Dated	Program Dates	Station
9/15/93	3/18/93-5	KFBI-FM (Pahrump, NV)
(resubmission) 9/17/93	2/25, 3/1, 3/95	KFBI-FM (Pahrump, NV)
	3/17, 3/24, 3/29 4/12, 6/10, 6/16 6/22, 6/24, 6/28 7/1, 8/2, 8/13 8/16, 8/19, 9/6 9/7, 9/14, 9/20/93.	
10/25/93	9/7, 9/14, 9/17	KFBI-FM (Pahrump, NV)
	9/20, 9/21, 9/22 9/27, 9/28, 9/30 10/18/93.	
12/25/93	10/1, 10/4, 10/5	KFBI-FM (Pahrump, NV)
	10/6, 10/12/93.	
12/28/93	12/27/93.	KFBI-FM (Pahrump, NV)

One complaint, dated November 11, 1993, concerning material aired during the Howard Stern show by WXRK-FM (New York, NY), on August 4, 1993, was filed pseudonymously by "Susan Jones."

[14] *See Infinity Broadcasting Corporation*, FCC 94-26 (adopted January 31, 1994), which identifies the specific material that we believe is actionably indecent under existing Commission standards.

dressed in a rulemaking proceeding. Accordingly, we will exercise our discretion, at this time, to limit our response to these latest broadcasts to monetary forfeitures.

Having fully considered the allegations and contentions presented in AFA's and ART's informal objections, we find that no substantial and material question of fact has been raised with respect to Infinity's qualifications to be or to remain a Commission licensee. We further find that grant of the above-referenced application will serve the public interest, convenience and necessity. This action is without prejudice to any actions the Commission may deem appropriate should Infinity broadcast indecent material in the future.

Accordingly, the petition to deny filed by Americans for Responsible Television IS HEREBY DISMISSED and, when considered as an informal objection, IS HEREBY DENIED, the informal objections filed by the American Family Association and Diane Vudmaska ARE HEREBY DENIED, and the above-referenced application, BALH-930618GE, IS HEREBY GRANTED.

This letter was adopted by the Commission on January 31, 1994.

BY DIRECTION OF THE COMMISSION*

William F. Caton
Acting Secretary

Attachments

*Chairman Hundt not participating; Commissioner Quello dissenting and issuing a statement; Commissioner Duggan issuing a statement.

Dissenting Statement of Commissioner James H. Quello

In re: KRTH(FM), Los Angeles, CA Assignment of License

The pattern of egregious repeated violations of FCC indecency rules is so flagrantly aggravated by six new complaints against Infinity and Howard Stern that I am impelled to dissent to being a party to any action that would result in approving additional stations for Infinity. This is such a serious nationwide matter that I believe final disposition of the Infinity case should involve a thorough review by a full Commission. Once the issues raised in the Act III court case have been fully addressed, the full Commission should reconsider Infinity's repeated flaunting of the FCC indecency rules which could bear on the fitness of the licensee. It is apparent that previous FCC fines have not had a deterrent effect. Additional fines could merely be written off as a cost of doing business. In fact, no fines have been paid. Infinity is actively opposing the FCC fines exercising its legal rights. Approving transfer of additional stations to Infinity at this time might be misinterpreted as the FCC endorsing Infinity and Howard Stern actions.

The FCC has broad discretion in determining and implementing the public interest. I believe it is antithetical to the public interest to authorize additional stations for probable dissemination of gross indecency and possibly obscene broadcasts by Stern. It is unlikely and counter-intuitive to believe decent responsible people would find it in the public interest to support additional outlets for licensees propagating lewdness, incest, deviant behavior and demeaning women, blacks and gays. Certainly, First Amendment rights were not conferred by our Founding Fathers for repulsive indecent or possibly obscene purposes. It must surely be embarrassing for First Amendment absolutists to defend language quoted below, broadcast at times children and young people are in the audience.

In this case, substantial justice should ultimately prevail over any technical legalism that First Amendment purists may utilize. Substantial justice requires the FCC to serve overall public interest. Today there is an overwhelming public outcry against excessive, explicit, deviant sex and glamorized violence and brutality on the air. It requires responsible action by the FCC and by public service minded broadcasters.

I believe substantial and material questions of fact have been raised by the continued repeated egregious violations so as to question whether further grants of assignment applications to Infinity would serve the public interest, convenience and necessity.

RQ: Becoming a mother takes a toll on a woman's whole body.
HS: Yeah, what about their horny husbands?
RQ: After a month nearly half of the women surveyed in this study they did, said that they had breast problems.
HS: Yeah.
RQ: Including discomfort, infection and nipple irritation.
HS: Yeah, my wife's got all that.
RQ: Other common problems at one month included fatigue, hemorrhoids, constipation, poor appetite and hot flashes.
HS: Appetite she hasn't lost.
RQ: (Laughs) Oh, stop it, after three months 40 per cent reported sexual problems such as painful intercourse.
HS: Are their hands alright after, how about some action that way.
RQ: Decreased desire.
HS: She, you know, she went out and bought condoms.
RQ: Or difficulty reaching orgasm.
HS: She went out and bought condoms, my wife, you know, I bought condoms, but I know she.
RQ: Nine out of five still have problems after delivery a year later.
HS: Yeah, how are their mouths?
RQ: Oh stop it.
HS: Okay, I mean, you know, I'm sensitive to all that stuff you just read. But how are their hands and mouths? Fine, right?
RQ: They're tired too.
HS: Oh, I see. Take a nap is right. Got a housekeeper, take a nap.
RQ: Oh, you're so understanding.
HS: Get your hand and mouth ready.

HS: I go over to him, let me see it. He starts pulling his pants off. Look at this. I thought he was going to show me, you know, his nuts. I don't know what he was going to show me. And then he pulls his underpants to the side and he shows me this whole, green, globby mess.

RQ: She's in love, yeah.
HS: So she had to sleep next to me, so she comes in at midnight, bangs open the door, I'm wide awake, I got no sleep last night.
RQ: Oh no.
HS: I'm up and she's snoring away in the bed. I went downstairs to masturbate.
AS: Oh get out.
HS: I did and you know, this is after making love to my wife.
RQ: Oh, you're a hero.

RQ: See how good they are? They survive.
HS: They're strong.

HS: This is the one about incest? Daughter?
RQ: Let me hear that.
HS: I want to have sex with my daughter.
RQ: That's romantic.
HS: It's romantic too. It's a ballad to my daughter. (Laughter) You're so cute in your jammies, I don't know what I'm saying, I know Jerry Lee Lewis is with his cousin but.
RQ: Daughters too close.
MV: (Unintelligible) Breakfast table in an otherwise empty room, beyond her.
HS: This is going to be a big hit this one.
MV: My only.
HS: This guy goose bumps.
MV: That are ever. (Unintelligible)
HS: My thick fingers will make you happier than Barney. I know, yeah.
MV: (Unintelligible)
HS: Yeah, they're good.
RQ: Yeah, where's my copy?
MV: I'll bring it tomorrow.
HS: I'll take this one home, before Robin grabs it from me, she's wrestling me. This one's about getting it on with your father. Guys.
RQ: Daughters.
HS: No, this is guys who get it on with their dads.
RQ: I see.
HS: I love you dad, you're my dessert, every night. This is good.
MV: (Unintelligible) That's okay man cause I love.
RQ: (Unintelligible) Played this one before.
HS: Why don't those dudes come on my show? Let's come down here and be naked.

Stern to female caller:

25. "Am I gonna eat you up when I see you?"
26. "I'd like to take a bite out of your ass"
27. "Have you had guys bite your ass"
28. "Does it smell"
29. "What color are your panties, look down"
30. "Do you touch yourself in church"
31. "Do you ever look at yourself naked in front of a mirror"
32. "What size are your breasts" Do you ever wear a bra?" Do you wear an 'A,' 'B' or 'C' cup?"

33. "You big pussy"
34. "Why do you wear panties and a bodysuit, the stench?"
35. "Do you really get off in bed"
36. "I'm gonna kick your ass, you Pussy boys"
37. "Stupid Dickheads"
38. "This time we bury your ass"

A few sample excerpts from many previous violations:

[Discussing Kathy Lee Gifford]

HS: From your heart. She didn't reach into, she always, you know, you notice everything about her now, she's reaching into toilets.
RQ: Yes. Or somebody's reaching in for her.
HS: First, listen to this woman, first she loses her jewelry in the toilet, which I don't know how that happened, then she, she pees in the toilet and she has an assistant reach in and grab the watch out of the toilet.
RQ: Right. Right, she doesn't go get it herself.
HS: Yeah. Some guy reached into her pee to get a (water sound effect) toilet. You know, to get a, to get her watch. Then, now the next story is that she'd have you believe, she's having a miscarriage, so she reaches in the toilet like that's a baby in there.
* *
HS: Yeah, you know, I, you know, when I make a bowel movement it is so perfect, I just can't bear to see it go down the toilet, you know it, it's Kathy Lee's bowel movement. It might be worth something. So I reach in and I grab it.
RQ: You know Reg, I'm saving every one of those.
HS: You know what, if I saved every one of my bowel movements we could auction them off on the show. Probably make a ton of dough. I wouldn't have to do all those stupid commercials. I mean for God's sake. Can you imagine the balls on this, I've never heard a woman say you reach, I've never heard of anyone reaching into a toilet (water sound effect) for a bloody mess. And you don't even see like a head or, I mean you don't see anything.
RQ: No, it's like an ink blot.
HS: I cry when Frank, when Frank plays with himself and everything dries up and I realize that could have been a baby. (Laughter) I can't handle it. (Laughter) Who's she kidding?

HS: He was lubed up. He jams his finger into Tony O. Tony O felt like a woman raped. Tony goes, "how, how." He stayed

HS: That's brilliant. That's some defense. because there's a movie on there you're allowed to whip it out and spew that evil gunk all over everybody. Now, I don't know about you but I've heard people actually say that this is not a serious offense. He did not hurt anybody.

HS: The closest I came to making love to a black woman was, I masturbated to a picture of Aunt Jemima.
GR: Oh, come on.
HS: On a pancake box. (Laughter) All right? And that was it. And then I heard Aunt Jemima died in a plane crash.
GR: Were you really one of those two finger guys?
HS: Yeah. (Laughter) Yeah, Geraldo, oh boy. No, I did it right on her kerchief. (Laughter)

HS: When I go to a movie, I don't need a hail storm coming out of some guy's genitalia. And I see the Pee Wee's offense as being a serious one. Now I know people think I'm joking but I am absolutely not. If my daughters or my wife were in a movie theater and they came back with some pervert throwing a huge hail storm on to their backs.
RQ: Wouldn't you be upset?
HS: I'd sure as hell would. I'd beat the piss out of him.

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Separate Statement
of
Commissioner Ervin S. Duggan

In re Assignment of License of KRTH(FM), Los Angeles, CA

But for the need to clarify the impact of Action for Children's Television v. FCC, No. 93-1092 (D.C. Cir. Nov. 23, 1993) on the Commission's indecency enforcement policies, I would have denied the grant of this application. In addition, I would have supported the launching of an administrative hearing at the Commission to determine whether the pattern of enforcement actions incurred by Infinity Broadcasting Corporation raises fundamental questions about Infinity's fitness to remain an FCC licensee.

To take such action now, however, would not be prudent or responsible. The Commission must act with maximum regard both for Court decisions and for preserving this institution's long-term ability to continue enforcing against broadcast indecency. Accordingly, I am supporting the levying of an additional fine against Infinity for yet another indecency violation. I do so with the sincere hope that future Commissions will take seriously that we are acting "without prejudice to any actions the Commission may deem appropriate should Infinity broadcast indecent material in the future." See By Direction Letter at 7.

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Before the
Federal Communications Commission
Washington, D.C. 20554

PUBLIC NOTICE

Released: November 21, 1994

Report No. DS-1481

BIG LEO SATELLITE SERVICE:
AMENDMENTS ACCEPTABLE FOR FILING

Five applicants have filed complete, amended applications to construct and launch satellite systems in the "Big LEO" satellite service in response to the Report and Order in *Amendment of the Commission's Rules to Establish Rules and Policies Pertaining to a Mobile Satellite Service in the 1610-1626.5/2483.5-2500 MHz Frequency Bands*, FCC 94-261 (released October 14, 1994). Upon initial review, the Commission has found all five applications are acceptable for filing. The Commission reserves the right to return these applications, however, if upon further review, it determines that they are defective or not in conformance with its rules, regulations or policies.

Constellation Communications, Inc. — **File Nos. 9-SAT-LA-94, 10-SAT-AMEND-94**

Constellation Communications, Inc. (Constellation) has filed an application to launch its proposed LEO MSS system (*see* File Nos. 17-DSS-P-91(48) and CSS-91-013) and an amendment to operate it in accordance with the spectrum sharing plan adopted in the *Report and Order* using code-division multiple access (CDMA) techniques.

Mobile Communications Holdings, Inc. — **File No. 11-SAT-LA-94, 12-SAT-AMEND-94**

Mobile Communications Holdings, Inc. (MCHI) has filed an application to launch its proposed LEO MSS system (see File Nos. 11-DSS-P-91(6) and 18-DSS-P-91(18)) and an amendment to operate it in accordance with the spectrum sharing plan adopted in the *Report and Order* using CDMA techniques.

Loral/QUALCOMM Partnership, L.P. — **File Nos. 13-SAT-LA-94, 14- SAT-AMEND-94**

Loral/QUALCOMM Partnership, L.P. (LQP) has filed an application to launch its proposed LEO MSS system (*see* File Nos. 19-DSS-P-91(48) and CSS-91-014) and an amendment to operate it in accordance with the spectrum sharing plan adopted in the *Report and Order* using CDMA techniques.

Motorola Satellite Communications, Inc. — **File Nos. 15-SAT-LA-94, 16-SAT-AMEND-94**

Motorola Satellite Communications, Inc. (Motorola) has filed an application to launch its proposed LEO MSS system (*see* File Nos. 9-DSS-P-91(87) and CSS-91-010) and an amendment to operate it in accordance with the spectrum sharing plan adopted in the *Report and Order* using TDMA/FDMA techniques.

TRW Inc. — **File Nos. 17-SAT-LA-94, 18-SAT-AMEND-94**

TRW Inc. (TRW) has filed an application to launch its proposed LEO MSS system (*see* File Nos. 20-DSS-P-91(12) and CSS-91-015) and an amendment to operate it in accordance with the spectrum sharing plan adopted in the *Report and Order* using CDMA techniques.

Comments or petitions regarding these applications may be filed on or before **December 22, 1994**. Replies and oppositions may be filed on or before **January 3, 1995**.

AMSC Subsidiary Corporation (AMSC) has filed a technical amendment (File Nos. 19-SAT-LA-94 and 20-SAT-AMEND-94) to its pending applications (File Nos. 15/16-DSS-MP-91) -- proposing to construct a low-earth orbit system to operate in accordance with the spectrum sharing plan adopted in the *Report and Order* using CDMA techniques. AMSC has deferred its financial showing, as permitted in the *Report and Order*. Because its application is not complete, we will not accept comments or petitions regarding AMSC's amendment at this time.

All applications will be available for public inspection in the Public Reference Room at 2025 M Street, N.W., Room 6220, Washington, D.C. during its normal operating hours. Copies of these documents may be obtained from ITS, Inc., 2100 M Street, NW, Suite 140, Washington, D.C. 20037, (202) 857-3800. For further information, contact Kathleen Campbell at (202) 634-1624.

FEDERAL COMMUNICATIONS COMMISSION

Before the
Federal Communications Commission
Washington, D.C. 20554

GN Docket No. 93-252

In the Matter of

Implementation of Sections 3(n) and 332
of the Communications Act

Regulatory Treatment of Mobile Services

FOURTH REPORT AND ORDER

Adopted: October 20, 1994; Released: November 18, 1994

By the Commission: Commissioners Quello and Barrett issuing separate statements.

I. INTRODUCTION

1. On July 18, 1994, the Commission adopted a *Second Further Notice of Proposed Rule Making*[1] in which we sought comment on whether we should consider certain non-equity relationships to be attributable interests for purposes of applying the 40 MHz limitation on broadband Personal Communications Service (PCS) spectrum,[2] the PCS-cellular cross-ownership rules,[3] and a more general Commercial Mobile Radio Service, (CMRS) spectrum cap.[4] We also requested comment on whether any attribution rules we might adopt in this proceeding should apply differently depending on whether the applicant or licensee involved is a designated entity.[5]

2. Specifically, the *Second Further Notice* asked whether resale agreements, management contracts, and joint marketing arrangements that do not confer *de facto* ontrol on a party should be considered attributable because these interests may affect the incentive or ability of PCS and other CMRS licensees to compete vigorously in the marketplace or because they may affect the number of effective competing providers or the independence of pricing decisions by service providers.[6] The twenty parties filing comments in response to the *Second Further Notice*, and the eleven entities filing reply comments, are listed in the attached Appendices. In addition, we received *ex parte* comments from the Department of Justice and Pacific Bell and Pacific Bell Mobile Services. Since the close of the comment period, the Commission has released the Third Report and Order[7] in this docket. In that Order, we adopted a spectrum cap of 45 MHz on the combined ownership of broadband PCS, cellular radio, and Specialized Mobile Radio (SMR) licenses that are classified as CMRS. This spectrum cap is in addition to the existing 40 MHz cap on broadband PCS ownership and the PCS-cellular cross-ownership rules. The *Third Report and Order* also conformed the rules relating to station management and control for CMRS providers and stated that we would address whether standards regarding indicia of control in connection with CMRS management contracts should be further conformed or modified in the context of our examination of whether to attribute non-controlling management contracts.[8]

3. We want to ensure that the significant changes that will be occurring in wireless services produce a robustly competitive market with a diversity of efficient providers serving a variety of consumer needs. The value assigned to PCS licenses in our recent narrowband auction furnishes further evidence that the spectrum available for wireless services is limited and that entry into the mobile wireless service market will not be unlimited so that safeguards are needed to maximize competition among those who are granted licenses. To that end, the Commission has taken steps to prevent excessive aggregation of spectrum through our various spectrum caps and cross-ownership rules. The goal of these limitations is to ensure that a single entity will not have the ability to influence or control a large portion of the available mobile wireless spectrum and thereby undermine competitive pricing for wireless services. We conclude that for the same reasons that we adopted the spectrum caps, we will attribute towards the spectrum limitations management agreements and joint marketing agreements between licensees that confer the ability to determine or significantly influence price or service offerings. While such arrangements are considered attributable, they will not be prohibited by our rules so long as those with attributable interests remain below the various spectrum thresholds after considering all attributable spectrum.

4. We believe that management agreements, resale, and joint marketing arrangements can enhance the competitiveness of wireless service providers. Management agreements have been used in the SMR industry and have proven to be beneficial to the introduction of new technology such as trunked systems and new wide area systems. In certain

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[1] Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services, GN Docket No. 93-252, *Second Further Notice of Proposed Rule Making*, 9 FCC Rcd 4400 (1994) (*Second Further Notice*).

[2] *See* Amendment of the Commission's Rules to Establish New Personal Communications Services, GEN Docket No. 90-314, Second Report and Order, 8 FCC Rcd 7700 (1993) (*Broadband PCS Order*), *recon.*, Memorandum Opinion and Order, FCC 94-144, released June 13, 1994 (*Broadband PCS Reconsideration Order*) *further recon.*, Third Memorandum Opinion and Order, FCC 94-265, released October 19, 1994 (Broadband PCS Further Reconsideration Order).

[3] *Broadband PCS Reconsideration Order*, at para. 98-140.

[4] *See* Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services, GN Docket No. 93-252, Further Notice of Proposed Rule Making, 9 FCC Rcd 2863 (1994) (*Spectrum Cap Notice*).

[5] Small businesses, rural telephone companies, and businesses owned by members of minority groups or women (or both) are collectively referred to as "designated entities." *See* 47 C.F.R. §§ 1.2110, 24.720.

[6] *Second Further Notice*, at para. 5.

[7] Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services, GN Docket No. 93-252, Third Report and Order, FCC 94-212, released Sept. 23, 1994 (*Third Report and Order*).

[8] *Third Report and Order*, at para. 226.

contexts, however, we believe they may also be used to facilitate the exercise of market power and produce anticompetitive results.

5. In this Order, we are concerned with the effects on competition from non-equity arrangements. In the current wireless marketplace, we believe that joint marketing arrangements such as MobiLink and Cellular One can be beneficial to consumers. These types of arrangements facilitate roaming and brand identity without conferring the ability to set or significantly influence the price or service offerings of individual licensees. We believe, however, that there may be other joint marketing arrangements that may confer the ability to significantly influence price and service offerings. In these cases, we would consider those arrangements to be attributable and would be prohibited if a party to the agreement exceeded the applicable caps.

6. We are also concerned about the effects attributing such arrangements might have on the competitiveness of designated entities. We do not believe that there is a shortage of qualified entrepreneurs or managers for wireless systems. Therefore, we do not believe that considering management contracts attributable interests for purposes of spectrum caps will harm competition or efficiency, nor will it harm the ability of designated entities to find suitable expertise should they wish to do so. We expect that investor/manager agreements are one of many alternatives available to designated entities and do not believe that treating management agreements as attributable for designated entities in exactly the same manner for spectrum cap purposes as for other entities will hamper the competitiveness of designated entities. This does not mean, however, that these management agreements will be deemed "attributable" for purposes of the revenue thresholds in the entrepreneur's blocks.[9] Additionally, we note that this decision in no way restricts designated entities (or other licensees) from entering into management or joint marketing agreements with entities with no attributable interests in the same market.

7. For the reasons stated below, we conclude that it is not in the public interest to treat resale agreements as attributable interests for the purpose of applying CMRS multiple-and cross-ownership rules. We do find, however, that joint marketing arrangements, as defined below, between competitors in the same geographic area and certain management agreements should be treated as attributable interests for purposes of spectrum caps and pursuant to the rules and criteria we adopt in this Order.

II. DISCUSSION

A. Resale Agreements

8. In the Second Further Notice, we tentatively concluded that resale agreements should not be attributable, and the record strongly supports that initial finding. AMSC, RCA, Motorola, McCaw and other commenters agree with the Commission that a reseller cannot exercise effective control of the spectrum used to provide its service or reduce the amount of service provided over that spectrum.[10] GTE argues that resale activities can serve as a source of competition in many service and geographic markets.[11] AMTA agrees that resale arrangements increase the number of parties offering service in a marketplace without giving the additional parties any rights which could lead to an unauthorized transfer of control.[12] Pacific Bell concurs with this position and points out that in California there are four resellers with more than 20,000 customers each, approximately five to seven resellers with 4,000 to 10,000 subscribers and over twenty resellers with 1,000 to 3,000 subscribers. Pacific Bell contends that parties interested in both cellular resale and direct provision of PCS services would decline to participate in the resale business if doing so would limit their flexibility in pursuing PCS licenses. The result, Pacific Bell states, would be fewer resellers in competition with each other and with facilities-based cellular providers.[13]

9. NCRA cites Commission rule making proceedings on resale and shared use in which the Commission recognizes the benefits of unrestricted resale activity and acknowledges that its current resale policy furthers brand name competition, service availability, and the efficient allocation of spectrum resources.[14] CSI maintains that cellular resale is dependent on the management and pricing decisions of other parties -- namely, the licensed cellular carriers. It asserts that the resellers' lack of power over facilities, services, and pricing has frustrated the cellular resellers' ability to enhance the services they would like to provide.[15] Columbia PCS, in contrast to the other commenting parties, urges the Commission to establish some limit on the amount of capacity available for a single reseller. It is concerned that an entity otherwise ineligible to obtain additional spectrum in a market could obtain an exclusive right to lease the entire capacity of a licensee. Columbia claims that such an arrangement could facilitate warehousing of spectrum and could substantially reduce competition in a given market.

10. As stated above, we reached the tentative conclusion in the *Second Further Notice* that resale agreements should not be attributable for the purpose of applying spectrum caps. This initial finding was based on the inability of resellers to exercise substantial influence or effective control over the spectrum on which they provide service or to reduce the amount of service provided over the spectrum. We conclude that our tentative finding was correct. There is no evidence in the record upon which we could conclude that resale arrangements are likely to compromise the ability of CMRS carriers to compete in the wireless marketplace. The reseller does not have the capability to control the resold spectrum and the reseller has no power to dictate what services are offered by the licensee or the prices at which these services will be provided. Moreover, as many commenting parties indicate, resale agreements increase competition in the marketplace rather than to

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[9] *See* Implementation of Section 309(j) of the Communications Act, Competitive Bidding, PP Docket No. 93-253, Fifth Report and Order, FCC 94-178, released July 15, 1994, *recon.* Fifth Memorandum Opinion and Order, FCC 94-285, adopted Nov. 10, 1994.

[10] *See, e.g.,* AMSC Comments at 3; RCA Comments at 7; Motorola Comments at 9-10; McCaw Comments at 3-4.

[11] GTE Comments at 9.

[12] AMTA Comments at 10.

[13] Pacific Bell Comments at 2-3.

[14] NCRA Comments at 5, note 12.

[15] CSI Comments at 2.

lessen it. Parties have suggested that PCS licensees may wish to resell cellular service while they are building their PCS network in order to provide service to the public expeditiously.[16] We believe that resale activities are in the public interest because they expand the availability of communications services, promote the efficient use of spectrum, and enhance competition.

11. We also conclude that Columbia's concern that an entity might obtain exclusive right to lease the entire capacity of a licensee is unfounded because of the common carrier status of CMRS licensees. An exclusive capacity arrangement would not be permitted if it violates Section 202 of the Communications Act of 1934, as amended.[17] Section 202 provides that a common carrier must offer its facilities to the public on a basis that is not unjustly or unreasonably discriminatory. In such a situation, the carrier would have the burden of demonstrating that any such exclusive capacity arrangement does not unreasonably impede its ability to meet its common carriage obligations under Title II of the Act. While we recognize that CMRS providers may offer individualized or customized service offerings, we have stated our intention previously that if such offerings meet the definition of CMRS, they will be classified and regulated as CMRS.[18] The CMRS definition narrowly restricts the types of services that are not deemed to be available to the public and, consequently not common carrier services. Specifically, under the public availability prong of the CMRS definition, a service is considered not available to the public only if it is used for a licensee's internal use or Commission rules limit eligibility to specified user groups.[19] A customized or individualized service offering would meet the public availability prong of the CMRS definition and would be treated as a common carrier service if it meets the other prongs of the CMRS definition. Thus, any grandfathered private mobile radio service (PMRS) carrier who has entered into such exclusive capacity arrangements in the past will be required to satisfy common carrier standards at the end of the transition period. Similarly, carriers who may enter into such arrangements in the future will be subject to common carrier requirements.

B. Management Agreements

12. In the *Second Further Notice*, we expressed concern that non-equity relationships that do not rise to the level of *de facto* control nevertheless might merit attribution because they could raise anticompetitive concerns where the manager or marketer acquires special proprietary information about a licensee's customer base and pricing information or has significant influence on the licensee's competitive conduct. We sought comment on whether access to such information, if used in an anticompetitive manner, could lead to a reduction in choices for the consumer of communications services.

13. All but two of the commenters contend that making management agreements attributable interests is inappropriate and contrary to the public interest. BellSouth argues that control should be the sole factor for determining attribution of non-equity relationships and that any agreement that confers *de facto* or *de jure* control upon a party other than a licensee should be considered an attributable interest.[20] Simron, Nextel, DialPage, and other representatives of the SMR industry maintain that management agreements have been used in that industry for years and have contributed to its growth and success. Motorola also contends that management agreements in the SMR context have served to increase competition and diversity in the mobile services marketplace by providing a source of consultation, advice, and expertise to inexperienced licensees.[21] Entities representing the SMR industry are particularly concerned that such a change in Commission policy toward management agreements could injure numerous licensees that have relied on existing policies.

14. Several commenters point out that management agreements are likely to play a critical role in ensuring the successful launch of PCS and other services that will be offered by designated entities. They maintain that adoption of attribution rules for non-equity interests would have a chilling effect on opportunities for designated entities to enter the wireless communications business.[22] LCC asserts that designated entity participants need the broadest possible access to expertise and resources in order to compete effectively.[23] Pacific Bell alleges that competition will suffer if the expertise of experienced operators will no longer be available to less experienced licensees.[24] Moreover, argues Southwestern Bell, making management agreements attributable would have a negative impact on designated entities by foreclosing to other companies any significant management interest in the licenses held by designated entities.[25]

15. CTIA maintains that attribution rules for non-equity interests are not necessary because the Commission has already provided sufficient restrictions and conditions to ensure that no CMRS provider will exert market power by controlling large amounts of spectrum in a given geographic market, and to ensure that designated entities will be the real party in interest and not a front or sham operation.[26] Similarly, AMTA argues that existing rules and regulations are already in place which give the Commission the authority to halt any anticompetitive behavior.[27] Pacific Bell claims that the licensee has every incentive to scrutinize carefully any management agreement it enters into to ensure that the agreement will put it in the best

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[16] *See* In the Matter of Equal Access and Interconnection Obligations Pertaining to Commercial Mobile Radio Services , CC Docket No. 94-54, *Notice of Proposed Rule Making and Notice of Inquiry*, FCC 94-145, released July 1, 1994 at n.251.

[17] 47 U.S.C. §202.

[18] *See* Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services, in GN Docket No. 93-252, Second Report and Order, 9 FCC Rcd 1411, 1439 n.130 (1994) (*Second Report and Order*), *recon. pending*.

[19] *Second Report and Order*, 9 FCC Rcd at 1441, para. 68. A commercial mobile radio service is one that is 1) provided for profit, 2) interconnected to the public switched network, and 3) available to the public. *Id.* at 1425-1442. *See also* Communications Act, § 332(d)(1), 47 U.S.C. § 332(d)(1).

[20] BellSouth Reply Comments at 3.

[21] Motorola Comments at 6-7.

[22] *See, e.g.*, NYNEX Comments at 2; PlusCom Comments at 2; DialPage Comments at 4; GTE Comments at 6; McCaw Comments at 7.

[23] LCC Comments at 6.

[24] Pacific Bell Comments at 5.

[25] Southwestern Bell Comments at 7.

[26] w CTIA Comments at 4.

[27] AMTA Comments at 4.

competitive position possible. It also asserts that the Commission should not get involved in the "micromanagement" of business by defining what constitutes a management agreement. It maintains that engaging in this type of activity would be an administrative "nightmare" and would consume Commission resources without any real benefit.[28]

16. PCC does not support or oppose attribution with respect to non-equity relationships. Rather, it urges the Commission to refine the *Intermountain Microwave* control test.[29] In its view, the Commission cannot determine whether management agreements should be found to create attributable interests for application of any PCS or CMRS spectrum cap until it defines the types of management agreements that comply with the *Intermountain Microwave* criteria. PCC asserts that the communications environment of today is radically different than that of 1963 when *Intermountain Microwave* was decided. Because of today's complex technology, PCC maintains that the level of expertise and training required to construct, operate, and maintain such communications systems is much greater than in the past, and that the business and financial acumen needed to manage these systems has increased greatly. PCC contends that in this environment, the Commission should adopt control and real-party-in-interest criteria that are consistent with existing communications business practices.[30] Pacific Bell also argues that CMRS entrants need a clear understanding of the scope of the powers that may be exercised under management contracts consistent with the Commission's Rules.[31] Likewise, NABOB supports PCC's "safe harbor" guidelines, contending that guidance is necessary before entities begin entering into management agreements.[32] PRTC states that the control test under *Intermountain* should be applied in light of new technological developments and in the context of today's business environment.[33] On the other hand, Sprint disagrees that refinement of the *Intermountain Microwave* test is warranted. It argues that the *Intermountain Microwave* criteria provides adequate guidance to licensees concerning the circumstances under which the Commission would find that a *de facto* transfer of control has occurred.[34]

17. Columbia and the Department of Justice urge the Commission to consider non-equity interests as attributable for spectrum cap purposes. Columbia asserts that the Commission should adopt clearer guidelines regarding all forms of non-equity relationships and should narrowly define permissible management contracts to allow subcontracting arrangements for any specific functional task (*e.g.*, construction). Columbia argues that the Commission should not allow parties to enter into management contracts that are tantamount to a general contractor role because, in its view, such contracts would result in a *de facto* transfer of control. Although Columbia's plan would permit subcontractor arrangements, it would also make these arrangements attributable interests that would apply to designated entities and non-designated entities alike. In addition, Columbia contends that the Commission should require such subcontracts to be priced at fair market value. *Ex parte* comments from the Department of Justice express a similar concern. The DOJ is concerned that such non-equity relationships might raise competitive concerns, specifically where one of the parties to such agreements has the power to determine or affect significantly prices or service output for two or more CMRS licensees in the same geographic market. In such situations, the DOJ contends that the management firm effectively controls the competitive capabilities of both of those licensees, and thus can significantly constrain the scope of competition between them. It maintains that the potential for reduced competition from an agreement which allows a firm to determine or significantly affect prices or service offerings for two or more CMRS licensees is obvious when the agreement involves multiple licensees within a particular geographic market. Such an agreement could effectively create a single economic entity and virtually eliminate any possibility of meaningful competition in that market between the licensees subject to the agreement.[35] In response, Pacific Bell argues that the standard DOJ proposes is so vague that it may have the opposite effect and deter entities from entering into pro-competitive agreements. It urges the Commission to provide specific criteria regarding what provisions of an agreement constitute a substantial influence over prices or services.[36]

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[28] Pacific Bell Comments at 4, 6.

[29] PCC Comments at 4-8, citing *Intermountain Microwave*, 24 Rad. Reg. 7 (P&F) 983 (1963).

[30] PCC Comments at 3. In the context of management agreements, PCC asserts that adoption of certain criteria would eliminate the complex, time-consuming, fact-specific litigation now common in real-party-in-interest litigation. PCC suggests, for example, that we require the inclusion of provisions in management agreements that specify: that the licensee may remove the management company, without penalty, upon substantial misconduct or uncorrected violation of Commission rules; that the licensee must review and sign all applications, amendments, and similar filings with the Commission, and may require any changes it deems desirable in such documents; that the licensee may terminate the management contract within 10 years of its effective date or last renewal, without penalty; and that the management company may not hold a veto power over the licensee's powers under the agreement. PCC reasons that if the manager holds a *bona fide* ownership interest in the licensee, it should be limited to whatever power arises from its ownership interest and not receive additional powers of control over the licensee through the management agreement.

[31] Pacific Bell Reply Comments at 3.

[32] NABOB Reply Comments at 3-5.

[33] PRTC Reply Comments at 4. PRTC urges the Commission to clarify that "virtual network arrangements" would not result in interest attribution. It explains that, because of the expense involved, many new PCS/CMRS providers may seek to fit within existing networks rather than build their own stand-alone networks. PRTC explains that in such situations, the licensees may not physically control the overall network, but will control the use of their spectrum and will be able to activate and deactivate the customer premises equipment of customers. Moreover, it claims that the network manager would not have access to customer lists or similar competitive information. In light of the limited information provided by PRTC concerning these type of arrangements, and because the *Second Further Notice* did not seek comment on this matter, we are not able to address PRTC's concern at this time.

[34] Sprint Reply Comments at 6-7.

[35] DOJ *Ex Parte* Comments at 4.

[36] Pacific Bell Ex Parte Comments at 2.

18. In the *Second Further Notice*, we acknowledged that any agreement that confers on a party other than the licensee *de facto* control over a Commission-licensed facility would be considered an attributable interest and would violate Section 310(d) of the Act if the agreement has not been disclosed to and approved by the Commission in advance of consummation. We indicated that issues of *de facto* control are determined pursuant to existing precedent, citing the *Intermountain Microwave* decision.[37] In the *Third Report and Order* we stated that we would clarify our interpretation of *de facto* control for reclassified CMRS providers.[38]

19. We asked in the *Second Further Notice* that commenters address whether there are relationships that do not rise to the level of control that should be considered attributable interests because they may affect competition. Virtually all the commenters approached the issue as one of control and not whether adopting attribution rules in the absence of *de facto* control would deter anticompetitive conduct. *Ex parte* comments filed by the Department of Justice, however, did address the issue of treating non-equity agreements as attributable interests. Notwithstanding the views expressed by the majority of commenters, and because they did not address our stated competitive concerns, we have concluded, for the reasons discussed below and based upon our concerns about possible anticompetitive behavior, that it is in the public interest to make certain management agreements between or among competitors in the same geographic area subject to our CMRS multiple-ownership and cross-ownership rules.

1. Criteria for *de facto* transfers of control

20. We recognize that in the past, different criteria have been used to determine whether a private carrier or common carrier has relinquished control of its facilities. In 1985, the Private Radio Bureau issued an opinion addressing five petitions to dismiss several SMRS applications filed by Motorola. The petitions were based on allegations that Motorola, through the use of management contracts, had assumed *de facto* control of SMR systems licensed to Comven, Inc. in violation of Section 310(d) of the Communications Act. The Bureau determined that licensees may hire entities to manage their SMR systems, provided that the licensees do not "contract away their control of the system."

> This means that a licensee must have a bona fide proprietary interest in its system and that it exercise the supervision over the system that it requires consistent with its status as licensee.[39]

In the Common Carrier Bureau, the guidelines established in the *Intermountain Microwave* decision have been used to determine who controls a common carrier licensee.[40] Over the years, we have relied on the six factors addressed in the *Intermountain Microwave* decision to determine in particular cases whether an unauthorized transfer of control has taken place in violation of Section 310(d) of the Communications Act.[41] In each case, we have found that the criteria are sufficient to enable us to review management contract terms (along with other arrangements such as options and rights of first refusal), to determine control issues and to furnish meaningful guidance to licensees in negotiating such agreements. Columbia, PCC, Pacific Bell and NABOB all suggest that the criteria established in *Intermountain Microwave* are no longer sufficient for determining whether a licensee has relinquished control of its licensed facilities. We, however, agree with Sprint, CTIA, BellSouth and PlusCom, that the guidelines set forth in *Intermountain Microwave* and its progeny provide workable standards for the Commission and licensees to use in assessing control issues. We believe that these established guidelines should apply to all CMRS providers, including reclassified PMRS carriers upon expiration of the transition period. Accordingly, we will continue to use the control factors set forth in the *Intermountain* decision when considering questions of *de facto* control of a CMRS licensee in particular cases. Extending these control criteria to all CMRS providers will promote regulatory consistency and conformity among these licensees. Although a few of the commenters suggest that we revise the *Intermountain* control factors, we decline to do so here. We also reject PCC's proposal to adopt certain "safe harbor" guidelines. Several of PCC's suggested criteria are concerned with contractual terms that are more appropriately negotiated by the parties in their agreements and not imposed by the Commission.

21. In the *Second Further Notice*, we also sought comment on how non-equity relationships should be construed in the context of determining whether the designated entity has *de facto* and *de jure* control of the licensee.[42] We received no comments addressing this matter in this proceeding. However, the issue of designated entity control was addressed upon reconsideration of our designated en-

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[37] *Second Further Notice*, at para. 5. *See also id.* at para. 5, note 7 (citation of authorities).

[38] *Third Report and Order*, at para 226.

[39] Applications of Motorola, Inc., File Nos. 507505 *et al.*, issued July 30, 1985 at para. 25. *See also Public Notice*, 64 RR 2d 840 (PRP 1988) restating guidelines.

[40] The Court of Appeals recently remanded two proceedings relating to determining issues of control. We note, however, that in handing down these two decisions, the Court was concerned not with the validity of the *Intermountain Microwave* criteria, but rather with the proper application of those criteria. *See* Telephone Data Systems, Inc. v. FCC, 19 F. 3d 655 (D.C. Cir. 1994), *vacating and remanding* La Star Cellular Telephone Co., 7 FCC Rcd 3762 (1992) and Telephone Data Systems, Inc. v. FCC, 19 F. 3d 42 (D.C. Cir. 1994), *vacating and remanding* Ellis Thompson Corp., 7 FCC Rcd 3932 (1992). On remand the Commission will be deciding how the existing *Intermountain Microwave* factors are to be applied in particular cases.

[41] The six factors are: (1) Does the licensee have unfettered use of all facilities and equipment? (2) Who controls daily operation? (3) Who determines and carries out the policy decisions, including preparing and filing applications with the Commission? (4) Who is in charge of employment, supervision, and dismissal of personnel? (5) Who is in charge of the payment of financing obligations, including expenses arising out of operating? and (6) Who receives monies and profits from the operation of the facilities? *Intermountain Microwave*, *supra*, note 29 at 984. *See also* Cellular Control Notice, 1 FCC Rcd 3 (1986); Public Notice, Common Carrier Public Mobile Services Information, "Mobile Services Division Releases Guidance Regarding Questions of Real Part in Interest and Transfers of Control for Cellular Applications," Report No. CL-93-141, Sept. 22, 1993; Public Notice, Common Carrier Public Mobile Services Information, "Mobile Services Division Releases Guidance Regarding Questions of Real Party in Interest and Transfers of Control for Cellular Applications in Markets Beyond Top 120," Report No. CL-87-1, Oct. 2, 1986.

[42] *Second Further Notice* at para. 4.

tity auction rules for broadband PCS adopted in the Fifth Report and Order in PP Docket No. 93-253.[43] Generally, where CMRS licenses are held by designated entities, such non-equity relationships with non-designated entities will be construed under the factors set forth in *Intermountain* and its progeny.

2. Attribution rules

22. An overriding purpose of the Omnibus Budget Reconciliation Act of 1993 is to promote the establishment of a more diverse and competitive communications marketplace.[44] We are concerned that such diversity may not exist when a single entity manages other licensees in the same geographic areas even when such entity does not "control" the licenses that it manages.[45] We agree with Columbia that a cellular company or a 30 MHz PCS licensee in a particular market that manages the operations of competing entities in that same market creates an opportunity for anticompetitive conduct to flourish. That management company may have access to sensitive information such as customer billing and collection accounts, customer lists, licensee pricing or other business plans or marketing strategies which can be used to impede competition in that market. In addition, we agree with the DOJ that the potential for reduced competition exists in an agreement which allows a management firm to determine or significantly influence prices or service offerings for two or more CMRS licensees.

23. These concerns apply as well to in-market management arrangements that may be made with designated entities. Several commenters have noted that designated entities are more likely to need the services of experienced CMRS providers, a point that we do not dispute. The anticompetitive concerns raised by management contracts, however, are equally applicable to all PCS spectrum blocks.[46] We believe that the benefits designated entities can receive from experienced managers can be achieved in full, without damage to the competitive balance of the market, if that manager is not a competitor in the same market. While we agree with NYNEX that management agreements could be structured to contain strict safeguards to prevent disclosure of sensitive information, the examination of various types of management contracts to ensure compliance would prevent the staff from expeditiously licensing PCS facilities. We believe that administrative efficiency requires adoption of a rule that provides a degree of certainty to applicants and licensees regarding the agreements that will be attributable. As described below, a designated entity may enter into an operations agreement with a CMRS licensee or a manager that has an attributable interest in another CMRS licensee in the same geographic area without having the interest imputed to such manager or licensee provided the manager does not determine (1) the nature or types of services offered by such licensee; (2) the terms upon which such services are offered; or (3) the prices charged for such services.

24. Our examination of the CMRS marketplace, and our evaluation of the record in this proceeding, lead us to conclude that reasonable attribution rules, tailored to minimize any intrusive consequences with regard to the operations of CMRS licensees, will serve as an important factor in promoting competition among CMRS providers. We have concluded that, in the absence of such attribution rules, there is a risk that certain types of management agreements may undermine our efforts to foster a competitive marketplace for wireless carriers. In order to ensure that the CMRS marketplace is competitive, thus fostering economic growth, promoting diversity among CMRS service providers, and enabling optimum access to the Nation's information infrastructure, we have concluded that attribution rules calibrated to curb potential anticompetitive behavior are necessary.

25. We therefore have decided to establish the following attribution rules and requirements. First, any person, as defined in the Communications Act,[47] who manages the operations of a broadband PCS, cellular, or SMR licensee pursuant to a management agreement shall be considered to have an attributable interest in such licensee, for purposes of applying the spectrum cap limitations established in the Commission's Rules, if such person, under the terms of the agreement, has authority to make decisions or otherwise engage in practices or activities that determine, or significantly influence, (1) the nature or types of services offered by such licensee; (2) the terms upon which such services are offered; or (3) the prices charged for such services. We point out that this rule applies to a person acting as a manager and exercising such authority whether the authority is exercised in his or her capacity as a manager or in any other capacity, *e.g.*, lender. We believe that this attribution rule, which triggers attribution *only* in cases in which anticompetitive conduct can reasonably be viewed as an outgrowth of a management agreement, minimizes any restrictive impact upon business operations but also furthers our goal of promoting competition in the CMRS marketplace.

26. Second, in cases where a licensee claims that a manager does not have an attributable interest in the license as a result of a management agreement, it shall be the responsibility of the licensee, in response to any request made by the Commission or in response to any petition or complaint filed with the Commission, to demonstrate that the procedures and practices that are established by the terms of the management agreement have been implemented to insulate the manager effectively from involvement in any activities of the licensee through which the manager could exercise the authority described in the preceding paragraph.[48] For purposes of evaluating any such

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[43] *See* n.9 *supra*.

[44] Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, Title VI, § 6002(b)(2)(A), 6002(b)(2)(B), 107 Stat. 312, 392 (1993).

[45] We consider two entities to be in the same geographic area when there is a 10 percent or greater population overlap of their respective licensed service areas. *See* 47 C.F.R. §§ 20.06, 24.204.

[46] Some commenters urge the Commission not to apply any attribution rules to specific classes of designated entities should the Commission adopt such attribution rules generally. For example, ROMGAT proposes that only 20 percent of the spectrum licensed to a qualified woman and/or minority-owned business should be attributable for spectrum cap purposes. ROMGAT Reply Comments at 7. RCA proposes that rural telephone companies be exempt from any rules that attribute non-equity relationships. RCA Comments at 9.

[47] Communications Act of 1934, 47 U.S.C. § 3(i).

[48] *See* note 59 *infra*.

demonstration, we expect that it will not be sufficient for the licensee to show that the management agreement merely contains a disclaimer or other provision indicating that the manager does not have any such authority, if the agreement fails to include specified procedures and practices designed to prevent the exercise of such authority. In instances where a manager serves in a dual capacity, *e.g.*, manager and lender, licensees must demonstrate that the manager does not exercise such authority in either capacity. Agreements entered into for the sole purpose of providing specialized technical products or services, such as telecommunications equipment, engineering services, network design services, legal and accounting services, billing services, construction, installation, repair as well as maintenance services or tariffed services such as high capacity "backhaul" links, shall not be subject to the requirements of this paragraph or the preceding paragraph. We do not believe that management agreements involving day-to-day technical and operational functions will result in attribution under our rules if the managing company does not engage in activities that determine or significantly influence prices or service offerings.

27. The principal purpose of the attribution requirements established in the preceding paragraphs is to ensure that aggregation of spectrum in a given geographic area does not result in anticompetitive influence over prices and service offerings. In order to accomplish this objective, we will take the following measures to achieve compliance with the attribution requirements. First, we note that the spectrum cap rules we have adopted[49] prohibit any person from having an attributable interest in CMRS licensees if the total amount of spectrum held by such licensees in the same geographic area would result in an aggregation of spectrum in excess of the limitations established in our rules.

28. Second, if a licensee enters into a management agreement that results in the manager under such agreement having attributable interests in licenses in excess of our spectrum cap limitations, then the licensee must take such actions as may be necessary to void the management agreement in a timely manner. Parties that currently have attributable management agreements may participate in PCS auctions on the condition that they bring such agreements that result in prohibited common interests into compliance with these rules within 90 days of a PCS license grant. The parties must also certify that they will comply with this requirement.[50] In the event that such an agreement went into effect, the licensee would be subject to appropriate enforcement actions by the Commission.[51]

C. Joint Marketing Arrangements

29. In the *Second Further Notice*, we sought comment on whether joint marketing agreements should constitute an attributable interest for the purpose of applying the spectrum aggregation caps. Under a joint marketing agreement, two or more CMRS providers would pool their resources to market their services to consumers. The opinion of most of the commenters is that these relationships are beneficial to both licensees and consumers. Motorola argues that joint marketing mechanisms allow small, independent operations to function cooperatively, thereby permitting them to obtain efficiencies otherwise reserved to larger competitors.[52] CTIA contends that marketing agreements can facilitate competition and customer acceptance of new PCS services by encouraging licensees to provide common features and services as a way of differentiating their service offerings from their competitors.[53] BellSouth also contends that joint marketing arrangements result in cost savings to service providers which can be passed on to consumers. It argues that the possible anticompetitive affects of such agreements can be dealt with by existing Commission rules and policies, and the antitrust laws.[54] GTE points out that because each licensee in a joint marketing arrangement always remains in control of its own facility, it is unlikely that such an arrangement would allow a competitor access to information that could be used for anticompetitive purposes.[55] Southwestern Bell urges the Commission to clarify that joint marketing arrangements do not encompass service mark and trademark licensing (*e.g.*, Cellular One, MobiLink) and interoperability agreements (*e.g.*, North American Cellular Network).[56] While it agrees that the types of joint marketing agreements listed by Southwestern Bell may have important procompetitive characteristics and should not be treated as attributable interests, the DOJ maintains that other joint marketing arrangements can raise anticompetitive concerns. According to the DOJ, the horizontal competitive concern in these agreements arises when one (or more) of the parties to the agreement controls a CMRS license in a market where, through the agreement, it also determines or significantly influences prices or service offerings for an additional license in that same market.

30. We agree with the DOJ that joint marketing arrangements can present anticompetitive concerns that can best be addressed by making marketing arrangements attributable interests where licensees enter into joint marketing if these agreements affect pricing or service offerings.[57] These interests will be attributed for purposes of the PCS aggregation limit, the cellular-PCS cross-ownership rules

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[49] *See* 47 C.F.R. §§ 20.6, 24.204, 24.229(c).

[50] *See Broadband PCS Further Reconsideration Order*, at para. 33; Section 20.6(e) and Section 24.204(f) of the Commission's Rules. The certification shall be included in the initial application filed for any CMRS license that is subject to these attribution rules. In the case of CMRS applicants whose applications were filed before the effective date of these attribution requirements, any such applicant may submit the required certification not later than 30 days after such effective date.

[51] *See, e.g.*, Second Report and Order, 9 FCC Rcd at 1430-31.

[52] Motorola Comments at 10-11.

[53] CTIA Comments at 9.

[54] BellSouth Reply Comments at 8.

[55] GTE Comments at 10.

[56] Southwestern Bell Reply Comments at 8. Southwestern Bell points out that Cellular One and MobiLink are service marks used by the cellular block A and block B band carriers, respectively, to denote compliance with certain service quality standards, as well as certain customer features. As Vanguard explains, a carrier's right to use the service mark is strictly geographically delineated by private contract. Although there may be some incidental overlap in marketing, parties to the Cellular One service mark do not pool resources to sell their service to customers in a single market. Because only Block A carriers participate, there cannot be any meaningful overlap between service areas of parties to the Cellular One service mark agreement. Vanguard Comments at 3-4. Similarly, interoperability agreements denote to customers that automatic roaming and automatic call delivery will be available throughout the country from those carriers who are signatories. Southwestern Comments at 8.

[57] *See* 47 C.F.R. §§ 20.6 and 24.204.

and the CMRS spectrum cap.[58] The rule will apply to designated and non-designated entities alike. Although we recognize that there may be benefits and cost savings from joint marketing agreements, we are concerned that such arrangements could effectively create a single economic entity substantially restraining meaningful competition in a geographic area where a single entity has an attributable agreement with two or more CMRS licensees, or where multiple CMRS licensees are parties to a single agreement. The commenters failed to provide evidence to the contrary. It should be noted that like management agreements, joint marketing agreements are not prohibited, but merely attributable. Thus, a 30 MHz PCS licensee may, for example, enter into a joint marketing agreement with a 10 MHz PCS licensee within its service area.

31. As with management agreements, we have decided to establish the following attribution rules and requirements for licensees entering joint marketing agreements. First, any licensee who enters into a joint marketing arrangement with a broadband PCS, cellular, or SMR licensee shall be considered to have an attributable interest in such licensee, for purposes of applying the spectrum cap limitations established in the Commission's Rules, if such person, under the terms of the agreement, has authority to make decisions or otherwise engage in practices or activities that determine, or significantly influence (1) the nature or types of services offered by such licensee; (2) the terms upon which such services are offered; or (3) the prices charged for such services. We believe that this attribution rule, which triggers attribution *only* in cases in which anticompetitive conduct can reasonably be viewed as an outgrowth of a joint marketing agreement, minimizes any restrictive impact upon business operations but also furthers our goal of promoting competition in the CMRS marketplace.

32. Second, it shall be the responsibility of a licensee with a joint marketing arrangement, in response to any request made by the Commission or in response to any petition or complaint filed with the Commission, to demonstrate that the procedures and practices that are established by the terms of the joint marketing agreement have been implemented to insulate effectively either party to the agreement from involvement in any activities of either licensee through which either party could exercise the authority described in the preceding paragraph.[59] For purposes of evaluating any such demonstration, we expect that it will not be sufficient for either licensee to show that the joint marketing agreement merely contains a disclaimer or other provision indicating that the parties do not have any such authority, if the agreement fails to include specified procedures and practices designed to prevent the exercise of such authority.

33. If any licensee enters into a joint marketing agreement that results in either licensee under such agreement having attributable interests in excess of our spectrum cap limitations, then that licensee must take such actions as may be necessary to void the joint marketing agreement in a timely manner. If any licensees currently have attributable joint marketing agreements, they may participate in PCS auctions on the condition that they bring such agreements into compliance with these rules within 90 days of a PCS license grant. Licensees with such agreements must certify that they will comply with this requirement.[60] In the event that such an agreement went into effect, the licensee would be subject to appropriate enforcement actions by the Commission.[61]

34. We agree, however, with Southwestern, Vanguard and RCA that the joint marketing agreements that constitute attributable interests should not include service mark and trademark licensing agreements, interoperability agreements and similar arrangements. As Southwestern explains, these types of agreements do not involve licensees in the same geographic area and do not create the concerns over pricing in-region service offerings overall or sharing of marketing and customer information that might tend to lessen competition in wireless markets.

III. CONCLUSION

35. As stated above, resale agreements will not be considered an interest attributable to a reseller in the context of a PCS spectrum aggregation cap, PCS-cellular cross-ownership restrictions, or a general CMRS spectrum cap. Typically, resellers cannot either exercise control over the spectrum on which it provides service or reduce the amount of service provided over that spectrum. Management and joint marketing agreements, however, present other concerns. Because certain management agreements and joint marketing arrangements may have an adverse impact on competition, we have decided to treat as attributable agreements that give a party to the agreement the power to determine prices or service offerings for more than one licensee in the same geographic area. We believe that the inclusion of such interests as attributable will not delay the licensing of broadband PCS services or hamper the rapid deployment of PCS to the public. The adoption of clear, unambiguous rules will eliminate the need for burdensome review and reporting requirements. We believe that these attribution rules will serve to promote vigorous competition and deter anticompetitive behavior.

IV. PROCEDURAL MATTERS; ORDERING CLAUSES

36. The analysis pursuant to the Regulatory Flexibility Act of 1980 is contained in Appendix C.

37. Accordingly, IT IS ORDERED that the rule changes as specified in Appendix D ARE ADOPTED.

38. IT IS FURTHER ORDERED that the rule changes made to Part 20 of the Commission's Rules herein WILL BECOME EFFECTIVE on January 2, 1995. This action is taken pursuant to Sections 4(i), 7(a), 302, 303(c), 303(f),

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[58] This rule is entirely consistent with the Commission's rules governing radio ownership and local "time brokerage," or joint programming arrangements where certain such arrangements are counted toward local and national multiple ownership rules. *See Revision* of *Radio Rules and Policies*, 7 FCC Rcd 2755, 2788-89 (1982), *on recon.* 7 FCC Rcd 6387, 6402 (1992); 47 C.F.R. § 73.3555(a)(2).

[59] We make clear that we will in no way condone frivolous complaints to the Commission that a specific management agreement or joint marketing agreement is in violation of the Commission's rules pursuant to this Order. Moreover, we emphasize that the Commission's initiation of an investigation into the allegations set forth in the complaint will not result in the automatic termination of the subject agreement or suspension of the construction or the operation of a licensee's facilities pending a Commission decision with respect to the complaint.

[60] *See* note 49, *supra*.

[61] *See* note 50, *supra*.

303(g) and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. Sections 154(i), 157(a), 302, 303(c), 303(f), 303(g), and 303(r).

39. IT IS FURTHER ORDERED that the rule changes made to Part 24 of the Commission's Rules herein WILL BECOME EFFECTIVE immediately upon publication in the Federal Register.[62] This action is taken pursuant to Sections 4(i), 7(a), 302, 303(c), 303(f), 303(g) and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. Sections 154(i), 157(a), 302, 303(c), 303(f), 303(g), and 303(r).

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

APPENDIX A

LIST OF PARTIES FILING COMMENTS

Party (and Short Title)

American Mobile Satellite Corporation (AMSC)

American Mobile Telecommunications Association, Inc. (AMTA)

Cellular Service, Inc. (CSI)

Cellular Telecommunications Industry Association (CTIA)

Columbia PCS, Inc. (Columbia)

Dial Page, Inc. (Dial Page)

GTE Service Corporation (GTE)

LCC, L.L.C. (LCC)

McCaw Cellular Communications (McCaw)

Motorola, Inc. (Motorola)

National Cellular Resellers Association (NCRA)

Nextel Communications, Inc. (Nextel)

NYNEX Corporation (NYNEX)

Pacific Bell Mobile Services (Pacific Bell)

PCC Management, Corp. (PCC)

PlusCom, Inc. (PlusCom)

Rural Cellular Association (RCA)

Simron, Inc. (Simron)

Southwestern Bell (Southwestern)

Vanguard Cellular Systems, Inc. (Vanguard)

[62] Entities with attributable agreements may participate in broadband PCS auctions provided that they bring such agreements into compliance with Commission rules. The rule changes adopted herein provide all parties with greater certainty about the attribution requirements of our CMRS rules. These benefits will be compromised unless the rule changes become effective immediately upon publication in the Federal register, because the deadline for filing applications to participate in the initial broadband PCS auction is October 28, 1994. Thus, there is good cause to order the changes to take effect upon Federal Register publication. *See* 5 U.S.C. §§ 553(d)(1), (d)(3).

APPENDIX B

LIST OF PARTIES FILING REPLY COMMENTS

BellSouth Corporation, Bell South Telecommunications, Inc., BellSouth Cellular Corp., and Mobile Communications Corporation of America (BellSouth)

Motorola, Inc. (Motorola)

Nextel Communications, Inc. (Nextel)

Pacific Bell Mobile Services (Pacific Bell)

Puerto Rico Telephone Company (PRTC)

The National Association of Black Owned Broadcasters, Inc. (NABOB)

The National Telephone Cooperative Association (NTCA)

Romgat Communication, L.P. (ROMGAT)

Simron, Inc.

Southwestern Bell Corporation

Sprint Corporation (Sprint)

EX PARTE COMMENTS FILED

The Department of Justice (DOJ)

Pacific Bell and Pacific Bell Mobile Services

APPENDIX C

Final Regulatory Flexibility Analysis

Pursuant to 5 U.S.C. Section 603, an initial Regulatory Flexibility Analysis was incorporated in the Second Further Notice of Proposed Rule Making in GN Docket No. 93-252. Written comments on the proposals in the Notice, including the Regulatory Flexibility Analysis, were requested.

A. Need for and Objective of Rules

1. This rule making proceeding was initiated to implement Sections 3(n) and 332 of the Communications Act of 1934, as amended. In prior orders, the Commission has adopted spectrum caps and cross-ownership rules to prevent excessive aggregation of spectrum. The goal of these limitations is to promote competition by ensuring that the aggregation of spectrum in a given geographic area does not result in anticompetitive influence over price or service offerings. The *Fourth Report and Order* in GN Docket No. 93-252 adopts attribution rules that make certain management agreements and joint marketing arrangements attributable interests for purposes of applying the Commission's spectrum cap rules. In the absence of such attribution rules, there is a risk that management agreements and joint marketing agreements may undermine our efforts to foster a competitive marketplace for wireless services.

B. Issues Raised by the Public in Response to the Initial Analysis

2. No comments were submitted specifically in response to the Initial Regulatory Flexibility Analysis.

C. Significant Alternatives Considered

3. The rules adopted in this *Order* are narrowly tailored to minimize any intrusive consequences with regard to the operations of CMRS licensees. The *Order* does not prohibit management or joint marketing agreements. It finds, however, that certain management or joint marketing agreements will be treated as creating attributable interests in the licensees for purposes of the Commission's spectrum cap limitations. The regulatory burdens we have established for all CMRS licensees, including small entities, are necessary to carry out our duties under the Communications Act of 1934, as amended. We will continue to examine alternatives in the future with objectives of eliminating unnecessary regulations and minimizing any significant impact on small entities. A copy of this *Order* will be sent to the Chief Counsel for Advocacy of the Small Business Administration.

APPENDIX D

PART 20 - COMMERCIAL MOBILE RADIO SERVICES

1. The authority citation for Part 20 continues to read as follows:

Authority: Secs. 4, 303, and 332, 48 Stat. 1066, 1082, as amended; 47 U.S.C. 154, 303, and 332, unless otherwise noted.

2. Section 20.6 is amended by adding a new Section 20.6(d)(9) and 20.6(d)(10) as follows:

* * * * *

(d) * * *

(9) Any person who manages the operations of a broadband PCS, cellular, or SMR licensee pursuant to a management agreement shall be considered to have an attributable interest in such licensee, if such person, or its affiliate has authority to make decisions or otherwise engage in practices or activities that determine, or significantly influence, (1) the nature or types of services offered by such licensee; (2) the terms upon which such services are offered; or (3) the prices charged for such services.

(10) Any licensee or its affiliate who enters into a joint marketing arrangements with a broadband PCS, cellular, or SMR licensee, or its affiliate shall be considered to have an attributable interest, if such licensee, or its affiliate has authority to make decisions or otherwise engage in practices or activities that determine, or significantly influence, (1) the nature or types of services offered by such licensee; (2) the terms upon which such services are offered; or (3) the prices charged for such services.

3. Section 24.204 is amended by adding a new Section 24.204(d)(2)(ix), 24.204(d)(2)(x) and by revising Section 24.204(f) as follows:

(d) * * *

(2) * * *

(ix) Any person who manages the operations of a broadband PCS or cellular licensee pursuant to a management agreement shall be considered to have an attributable interest in such licensee, if such person, or its affiliate has authority to make decisions or otherwise engage in practices or activities that determine, or significantly influence, (1) the nature or types of services offered by such licensee; (2) the terms upon which such services are offered; or (3) the prices charged for such services.

(x) Any licensee who enters into a joint marketing arrangement with a broadband PCS or cellular licensee, or its affiliate, shall be considered to have an attributable interest, if such licensee has authority to make decisions or otherwise engage in practices or activities that determine, or significantly influence, (1) the nature or types of services offered by such licensee; (2) the terms upon which such services are offered; or (3) the prices charged for such services.

* * * *

(f)* * *Provided, however, that these divestiture procedures shall be available only to: (i) parties with controlling or attributable ownership interests in cellular licenses where the CGSA(s) covers 20 percent or less of the PCS service area population; (ii) parties with attributable interests solely due to management agreements or joint marketing agreements; and (iii) parties with non-controlling attributable interests in cellular licenses, regardless of the degree to which the CGSA(s) covers the PCS service area population. * * *

SEPARATE STATEMENT

OF

COMMISSIONER JAMES H. QUELLO

Re: ***Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services (GN Docket No. 93-252)***

In this *Fourth Report and Order* we establish the generic rules for determining whether certain types of management and joint marketing agreements will be deemed attributable for purposes of the Commission's spectrum ownership caps in the Commercial Mobile Radio Service (CMRS). In so doing, this Commission is required to balance the potential for anti-competitive behavior against the business needs faced by the smallest potential players in a new industry, the "Designated Entities" (DEs), in a highly competitive capital and technical market.

This *Fourth Report and Order* deems resale agreements non-attributable for PCS, cellular and SMR services; however, management and joint marketing agreements will be treated as attributable in all cases for the purpose of applying the CMRS ownership limits. I can support this distinction only because the scope of the attribution of management and joint marketing agreements is limited to those exercising actual control in the same geographic market. Also, service mark and trademark licensing agreements and interoperability agreements are not deemed to be marketing agreements so they are not attributable.

I support *this Fourth Report and Order*, with some qualifications, in large measure because I whole-heartedly support the overarching goal of this Commission to foster a competitive market in the provision of the most advanced communications technologies, that is, in Commercial Mobile Radio Services such as Personal Communications Services (PCS). I am concerned, however, that we do not give with one hand by providing incentives for DEs to participate, while taking away with the other by limiting the flexibility that DEs require in raising capital and building and managing their systems.

I believe that the challenges that confront the DEs are real and substantial. They could well prove insurmountable unless this Commission is ever vigilant to guard against erecting additional road blocks to the construction of the much ballyhooed information superhighway.

As a fundamental premise, I believe that participation in new technologies such as PCS will be a big money undertaking. Licensees will expend large amounts of money not only to acquire

the license under the new scheme of competitive bidding but then, if they are the winning bidder, will immediately disgorge more money to acquire equipment and build the infrastructure. They will then need to market and operate their system.

In addition to access to financial resources, potential competitors -- especially the Designated Entities -- need access to technical and management expertise. The overwhelming majority of commenters contend that such non-equity interests should not be attributable. I agree with the almost universal majority of the commenters that discern substantial and proven benefits in permitting, indeed, in encouraging, management and joint marketing agreements. This Commission has other and more than adequate means available; in fact, we have other rules in place to guard against potential, but as yet merely speculative, anti-competitive behavior.

I am fully aware that the Department of Justice responded with filed comments that raise the specter of anti-competitive concerns. These comments were fully considered, as are all comments under the Commission's rules of procedure and the Administrative Procedure Act. I do not believe, however, that any particular comments should be accorded undue weight. Conversely, we should not disregard any properly filed comments based on their source. To argue that the commenters are "interested parties" is to state a truism. That a party filing comments is interested in the outcome of the proceeding is a reflection of the proper functioning of our administrative processes. Thinly veiled *ad populum* assertions obscure the issue; they do not denigrate the validity of concerns expressed in a party's comments.

It is for this Commission to establish policy and concordant regulations on matters within our jurisdiction. The purpose of the notice and comment process is to fully inform an independent regulatory agency such as the Federal Communications Commission in the exercise of such policy making functions.

Where policy objectives conflict, I believe that the Commission should retain maximum flexibility in setting forth our rules. Here, we balance the goal of deterring anticompetitive behavior against the goal of providing incentives for wider participation in the ownership of entities providing advanced communications services. I support this *Fourth Report and Order* because the decisions made herein are an integral part of the overall effort by this Commission to facilitate the introduction of advanced communications services into the economy for the benefit of American citizens. I remain concerned, however, that we may have disallowed management tools that have proven valuable in the past and would have been beneficial to Designated Entities in operating their systems successfully over the long term.

SEPARATE STATEMENT

OF

COMMISSIONER ANDREW C. BARRETT

Re: Implementation of Sections 3(n) and 332 of the Communications Act, Fourth Report and Order (GN Docket No. 93-252)

Today, we adopt rules that will treat certain types of management and joint marketing agreements as attributable interests in Commercial Mobile Radio Service (CMRS) licensees for purposes of the Commission's spectrum ownership caps. While I support the Commission's endeavors to deter anticompetitive behavior in the wireless communications industry, I am concerned that the Commission, by this decision, does not create uncertainty in the capital market at a time when businesses, and in particular, businesses owned by designated entities (DEs) are attempting to form strategic partnerships and alliances for the provision of these services.

In June 1994, the Commission adopted its "Competitive Opportunity Plan" and provided additional incentives in an attempt to ensure that designated entities have at least a realistic opportunity to participate in providing broadband Personal Communications Services (PCS). At that time, I indicated that the Commission's auction rules decision balanced the various goals of Section 309(j) of the 1993 Omnibus Budget Reconciliation.[1] I was particularly encouraged by the rules' flexibility as a means of: (1) enhancing the ability of capital markets to clearly evaluate the incentives created for investment in businesses owned by designated entities and (2) increasing the probability of participation by designated entities as PCS applicants. Unfortunately, I am concerned about the potential for confusion between designated entities and possible strategic partners that could result from this decision.

The majority of commenters opposed the attribution of management agreements--primarily because of the potentially adverse impact on designated entities. Despite these concerns, the Commission has opted, for public interest reasons, to deter anticompetitive behavior by wireless providers by attributing certain types of agreements for purposes of the spectrum cap. I hope that this decision does not adversely impact a designated entity's ability to form strategic alliances or to acquire

[1] See, Separate Statement of Commissioner Andrew C. Barrett, Implementation of Section 309(j) of the Communications Act-- Competitive Bidding (PP. Docket No. 93-253), June 29, 1994.

necessary capital for the provision of wireless services.

Management agreements will likely play a critical role for designated entities that seek access to resources that will enable them to compete effectively in the marketplace. We have attempted to set forth those agreements that will not be deemed attributable under the CMRS spectrum cap. Despite our sensitivity to the need for clarity, I hope that these rules do not erect another de facto barrier to entry for designated entity participation.

Finally, I believe that the Commission must balance its policy objectives with sufficient regulatory flexibility for designated entities. I support this item today as an effort to advance the introduction of new wireless services in the marketplace. However, I hope that the Commission will endeavor to make certain that these attribution rules do not hinder capital formation and strategic alliance initiatives.

Before the
Federal Communications Commission
Washington, D.C. 20554

CC Docket No. 94-136

In re Application of

ELLIS THOMPSON CORPORATION File No. 14261-CL-P-134-A-86

For facilities in the Domestic Public Cellular Radio Telecommunications Service on Frequency Block A in Market No. 134, Atlantic City, New Jersey

MEMORANDUM OPINION AND ORDER AND HEARING DESIGNATION ORDER

Adopted: November 18, 1994; Released: November 28, 1994

By the Commission:

I. INTRODUCTION

1. This memorandum opinion and order designates for hearing the application of Ellis Thompson Corporation (Thompson) to construct and operate a cellular telephone system. We find that there are substantial and material questions as to whether a third party became a real-party-in-interest in the Thompson application contrary to the Commission's rules.[1] We take this action "pursuant to a decision of the United States Court of Appeals for the District of Columbia Circuit reversing and remanding our prior order upholding the grant of Thompson's application. *Ellis Thompson Corp.*, 7 FCC Rcd 3932 (1992), *aff'd in part and rev'd in part sub nom. Telephone and Data Systems, Inc. v. FCC*, 19 F.3d 42 (D.C. Cir. 1994).

II. BACKGROUND

2. Thompson was selected by lottery to construct and operate a cellular telephone system on frequency Block A (the non-wireline block) in Atlantic City, New Jersey. It is wholly owned by Ellis Thompson, a now 77 year-old retired welder living in Vancouver, Washington. Pursuant to the terms of a settlement agreement among applicants for the Atlantic City authorization (the CMS Settlement Agreement), Thompson is entitled to a 50.01 percent ownership interest in the Atlantic City authorization, while other parties are entitled to a 49.99 percent interest.

3. Questions regarding the control of Thompson arise from agreements entered into by Thompson with two parties, Telephone and Data Systems, Inc. (TDS) and American Cellular Network Corporation (Amcell). Shortly after the lottery in 1986, Thompson entered into a letter agreement giving TDS an option to purchase Thompson's interest after the cellular system was completed. The agreement (as amended) provided, among other things, that TDS' approval was required for agreements calling for expenditures by Thompson of $50,000 or more (paragraph 16 of the agreement).

4. In 1987, Amcell notified TDS that it had acquired a 36.01 percent interest in the Atlantic City authorization from the original minority parties to the CMS Settlement Agreement. Amcell informed TDS that, under a supermajority provision of the CMS Settlement Agreement (Section 3.4(b)), Amcell's consent was required before TDS could buy Thompson's interest.

5. Thompson thereafter entered into an agreement with Amcell under which Amcell would construct the Atlantic City system and operate it for at least ten years. In compliance with paragraph 16 of its agreement with TDS, Thompson submitted the management agreement for TDS' approval. TDS, however, refused to consent to the agreement.

6. Thompson, nevertheless, executed the management agreement with Amcell, and simultaneously, entered into two related agreements. Under the first, Thompson granted Amcell a contingent option to purchase its interest in the event that TDS did not exercise its purchase option. Under the second, Amcell agreed to indemnify Thompson if the Commission denied Thompson's application because it found the management agreement objectionable.

7. In pleadings before the Commission's Common Carrier Bureau, Amcell challenged the propriety of paragraph 16 of the TDS agreement, while TDS challenged Amcell's rights under Section 3.4(b) of the CMS Settlement Agreement. Each asserted that the other's provision violated 47 U.S.C. § 310(d), which requires Commission consent to transfers of control of a license or construction permit. The Bureau upheld Section 3.4(b) but required the abrogation of paragraph 16. *Ellis Thompson*, 3 FCC Rcd 3962 (Mob. S. Div. 1988), *aff'd*, 4 FCC Rcd 2599 (Com. Car. Bur. 1989).

8. On review before the Commission, TDS supplemented its allegations against Amcell. TDS asserted that the management agreement, contingent option agreement, and indemnification agreement, taken together, indicated that Amcell had acquired control of Thompson.

III. COMMISSION ORDER

9. The Commission evaluated the control issue using the criteria set forth in *Intermountain Microwave*, 24 RR 983 (1963). *See also Public Notice*, 1 FCC Rcd 3 (1986), providing guidance regarding questions of control based on *Intermountain*. The six factors are these:

(1) Does the licensee have unfettered use of all facilities and equipment?

[1] Under 47 C.F.R. § 22.13(a)(1), applicants are required to disclose all real-parties-in-interest. Under 47 C.F.R. § 22.23 substantial changes in the beneficial ownership or control of applicants for cellular authorizations may result in their dismissal. *See also* 47 C.F.R. §§ 22.31, 22.918. Moreover, under 47 U.S.C. § 310(d) and 47 C.F.R. § 22.39 control over a cellular authorizations cannot be transferred without Commission approval.

(2) Who controls daily operations?

(3) Who determines and carries out the policy decisions, including preparing and filing applications with the Commission?

(4) Who is in charge of employment, supervision, and dismissal of personnel?

(5) Who is in charge of the payment of financing obligations, including expenses arising out of operating?; and

(6) Who receives moneys and profits from the operation of the facilities?

1 FCC Rcd at 3.

10. The *Intermountain* factors represent the normal incidents of responsibility for the operation and control of a common carrier facility. 24 RR at 984. As such, they generally provide useful guidelines for evaluating real-party-in-interest and transfer of control questions. For example, in the *Public Notice* cited above, the Commission explicitly adopted the *Intermountain* criteria as guidelines for questions arising from the use by cellular operators of management companies. We stress, however, that there is no exact formula for determining control and that questions of control turn on the specific circumstances of the case. *See Data Transmission Co.*, 44 FCC 2d 935, 936 (1974). Thus, in applying the *Intermountain* criteria, we examine the totality of the circumstances.

11. The Commission's analysis was as follows:

> *Use of the facilities.* Except for the shared Amcell switch, [Thompson] owns all the cellular equipment utilized in the Atlantic City system and is the lessee for all of the cell sites. Mr. Thompson also has access to the shared switch. Thus, it is clear that [Thompson], the licensee, has unfettered access to the system's facilities and equipment. Indeed, Mr. Thompson makes regular visits to the system. *Day-to-Day Operations.* While Amcell does manage day-to-day operations, such operations are subject to Mr. Thompson's ultimate supervision and control. Mr. Thompson approves the annual budget and major expenditures, receives periodic reports detailing the status of operations and maintains regular contact with the Amcell management team. [footnote omitted] *Policy Decisions.* Mr. Thompson is involved in making all major policy decisions and meets quarterly with Amcell management to discuss all aspects of the business over the past quarter and to discuss marketing and construction plans for the current quarter. While Amcell prepares FCC applications, they are reviewed by Mr. Thompson's independent FCC counsel, signed by Mr. Thompson and filed by his counsel. *Personnel Responsibilities.* Mr. Thompson is [Thompson's] only employee and determines his own salary, which is paid by [Thompson]. Although Amcell is [Thompson's] system manager and is thus responsible for hiring, firing and supervising personnel on a daily basis, Amcell itself is subject to dismissal for cause by [Thompson], which thus has the ultimate responsibility for personnel management. *Financial Obligations.* [Thompson] is financially responsible for the construction and operation of the Atlantic City cellular system. [Thompson] is liable on the loan from Provident Bank which has been used to meet the financial needs of the system. [footnote omitted] Moreover, while Amcell has authority to make payments on behalf of [Thompson] for operating expenses, Mr. Thompson must approve the annual budget for the system, any proposed expenditures outside the scope of the annual budget, and all checks in excess of $5,000, except for certain recurring payments for which the limit is $25,000. *Receipt of Monies.* All funds derived from operation of the cellular system are deposited directly into [Thompson's] separate bank account, to which Mr. Thompson has full access, and Amcell's management fees are paid out of that account. As majority owner, Mr. Thompson is ultimately entitled to 50.01 percent of the cellular system's proceeds. During the second quarterly meeting of 1990, Mr. Thompson ordered a cash distribution of system profits to the system's owners, commensurate with their respective interests.

7 FCC Rcd at 3935 ¶ 15. The Commission expressed concern that Amcell's undertaking to indemnify Thompson if the license is revoked would encourage a lax attitude on the part of the licensee. Nevertheless, the Commission found that a preponderance of the facts and circumstances indicated that there were no substantial and material questions of fact suggesting that Thompson had relinquished control. *Id.* at 3936 n.19.

IV. COURT OF APPEALS

12. On March 25, 1994, the United States Court of Appeals for the District of Columbia Circuit reversed and remanded. The court ruled that the Commission's application of the *Intermountain* factors was inconsistent with precedent in that the Commission, without explanation, treated them as a test of legal, rather than of *de facto*, control.

13. Reviewing the first four *Intermountain* factors, the court faulted the Commission for: (1) equating Thompson's "access" to the facilities it shares with Amcell with "use" of those facilities; (2) treating approval of major expenses and "contact" with Amcell management as "control of daily operations"; (3) considering "involvement" in major policy decisions as being the equivalent of "determining and carrying out" policy decisions; and (4) equating Thompson's right to nullify Amcell's personnel decisions with control over hiring and firing. The court was particularly troubled by a perceived inconsistency between the Commission's analysis of the control issue in this case and that in *La Star Cellular Telephone Co.*, 5 FCC Rcd 3286 (I.D. 1990), *aff'd*, 7 FCC Rcd 3762 (1992), and other cases.[2]

14. Following remand the parties were invited to comment on what further action should be taken. *Ellis Thompson Corp.*, 9 FCC Rcd 1888 (G.C. 1994).6X}Z [3]

[2] The court vacated and remanded the Commission's *La Star* decision for futher consideration. *Telephone and Data Systems, Inc. v. FCC*, 19 F.3d 655 (D.C. Cir. 1994). We have today adopted a further order in the *La Star* proceeding. *La Star Cellular Telephone Co.*, FCC 94- ( ).

[3] Before the Commission are: (1) comments, filed May 5, 1994,

V. COMMENTS

15. TDS contends that, in view of the court's opinion, the Commission cannot find that Thompson has *de facto* control over the cellular system. TDS argues that the Commission should order Amcell to divest its interest in the system and to abrogate Section 3.4(b). Thompson and Amcell respond that TDS' analysis represents an unduly mechanical application of the *Intermountain* criteria. They and PCC[4] argue that the Commission should take into account the realities of modern cellular telephone system operation in applying the *Intermountain* criteria. Specifically, they maintain that it is unrealistic to expect that Thompson will run the Atlantic City system as a "mom-and-pop" operation. Rather, these parties argue that the fact the Atlantic City system is a turnkey operation and a part of a regionally integrated system merely reflects current realities and should not be held against Thompson.

VI. ISSUE ANALYSIS

A. THE INTERMOUNTAIN FACTORS

16. We now turn to the specific *Intermountain* factors. We evaluate these factors bearing in mind the court's admonition that we must evaluate them in terms of actual and not theoretical control.

1. Use of the Facilities

17. *Comments.* Thompson and Amcell assert that Thompson owns all of the radio equipment associated with the cellular system and is the lessee of all of the cell sites.[5] They acknowledge that Thompson does not own the system's MTSO, which is owned by Amcell and is used in connection with Amcell's Wilmington, Delaware cellular system. They insist, however, that the sharing of switching facilities has been acknowledged by the Commission as a common attribute of cellular operation and does not reflect a lack of control. Moreover, they contend that appropriate control is also indicated by Thompson's free access to the switching facilities.

18. TDS argues that the common use of switching facilities by the Atlantic City system and Amcell's Wilmington system indicates an intention that the Atlantic City system be totally merged into Amcell's regional operations. TDS also argues that the court has ruled out treating Thompson's access to the switching facilities as an indication of control.

19. *Discussion.* The technical compatibility and capacity to integrate the Atlantic City system and Amcell's own cellular operations appears to be a key feature of the Thompson-Amcell relationship and appears to have potential impact on Thompson's unfettered use of the facilities. According to a description attached to the Thompson-Amcell management agreement, the Atlantic City system was designed to be "automatically" part of the "wide area Delaware Valley non wireline cellular system," which includes Amcell's Wilmington system and a Philadelphia, Pennsylvania system owned by Amcell's parent corporation. *See* Management Agreement, dated December 30, 1987, Schedule A "Outline System Configuration" at 2. The description indicates that technology used by the Amcell-related systems enables the Atlantic City system to be fully integrated with the other operations without additional hardware, software, or communications links. *Id.* This circumstance might reflect valid technical and financial advantages for Thompson and be consistent with Thompson's retention of unfettered use. It is also possible, however, depending on the totality of the circumstances, that the arrangement might reflect an intent for Amcell to exercise control over an integrated operation contrary to Thompson's unfettered use of the facilities. Thompson's reported access to the facilities does not address questions raised by the apparent importance given by the parties to the integration of the Atlantic City and Amcell-related systems. Nor does it indicate compliance with the "use" requirement of *Intermountain.* The evidence does not indicate that, as part of his access to the MTSO, Mr. Thompson is authorized to operate or otherwise use those facilities.

2. Day-to-Day Operations

20. *Comments.* Thompson and Amcell acknowledge that, under their management agreement, Amcell will oversee the day-to-day operations of the Atlantic City system. They assert, however, that this arrangement reflects a valid delegation of authority and that Thompson retains ultimate control over operations. They assert that: (1) Thompson conducts quarterly visits to the facilities and to Amcell's offices and maintains regular contact with Amcell management; (2) purchase orders, checks, and other documents requiring Thompson's approval are sent to an independent attorney for review; (3) Thompson approves the annual budget; (4) Thompson signs checks for non-recurring expenditures over $5,000 and all payments to Amcell and receives back-up information; and (5) Thompson reviews and approves all major contracts. They also submit that the

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by Thompson, Amcell, TDS, and PCC Management Corporation (PCC); and (2) reply comments, filed May 12, 1994, by Thompson and Amcell, and May 17, 1994, by TDS. We note that TDS is a party both to this proceeding and *La Star.* PCC is not a party to this proceeding or to *La Star.* We accept its comments as an *amicus.* The Common Carrier Bureau did not file comments in this proceeding and did not participate in the preparation of this order.

[4] PCC proposes that the Commission should update the applicability of the *Intermountain* criteria and approve "safe harbor" provisions for agreements between cellular licensees and management companies. Without here considering whether a general policy review in this area is warranted, none of PCC's specific proposals would justify a different outcome in this proceeding. In particular, we cannot, on the record of this case, rely on the parties' formal agreements alone, as PCC proposes in some situations, to make a meaningful assessment of *de facto* control. Nor would the adoption of PCC's suggested safe harbor provisions change the analysis here. Moreover, to the extent that the parties and PCC have called to our attention information about the current realities of cellular telephony, we have incorporated that information in our analysis. Such realities cannot, of course, change the requirements of Section 310(d).

[5] The service area of a cellular telephone system is divided into "cells." Users' mobile radio equipment communicates with a base station within the cell in which the user is located. The base stations are connected by land line to a mobile telephone switching office (MTSO), which is connected, in turn, to a switching office of the local telephone network.

management agreement is subject to an implied covenant which would permit Thompson to terminate the agreement for cause.

21. TDS questions whether Thompson maintains control over day-to-day operations. TDS contends that Thompson has no right to terminate Amcell's management for 20 years. TDS also notes that Mr. Thompson lives in Washington State, far from Atlantic City.

22. *Discussion.* We find that provisions of the management agreement raise questions as to Thompson's ability to effectively control day-to-day operations, which are not fully answered by Thompson's asserted manifestations of control. First, the agreement, as amended on September 8, 1988 (¶ 4A.9, as amended), provides that Amcell will manage the Atlantic City system for 10 years with an option to extend the agreement for two additional five-year terms. Thus, although Thompson may have some theoretical right to terminate the agreement for violation of an implied covenant, there is no provision that gives Thompson routine discretion to review or terminate Amcell's management for as long as 20 years. This factor may undermine Thompson's ability to exercise control over day-to-day operations.

23. Second, the November 23, 1990 amendment to the management agreement (¶ 1, ¶ 4A.4, as amended) provides that day-to-day operations of the Atlantic City system will be administered by Wilmington Cellular Telephone Company (WCTC), which also operates Amcell's Wilmington system. This seemingly complete integration of management between the two systems raises questions as to Thompson's ability to exercise control of day-to-day operations, since Thompson presumably has no right to control WCTC's activities to the extent that they relate to the integrated Wilmington system.

3. Policy Decisions

24. *Comments.* Thompson and Amcell detail what they assert are indicia of Thompson's control over policy matters. They explain that Mr. Thompson: (1) selected Amcell to manage the facility and negotiated the terms of the agreement with Amcell; (2) must approve litigation undertaken by Amcell; (3) was involved in policy determinations involving roamer arrangements, establishment of a retail center, and the revision of rates; (4) has quarterly meetings with Amcell; (5) has independent FCC counsel and counsel/business adviser; (6) has been actively involved in all major decisions and is regularly informed of major developments; (7) with the advice of independent counsel, executes and approves all filings; (7) approves budgets, directs proceedings, oversees marketing and pricing; and (8) in some instances has countermanded decisions by Amcell.

25. TDS urges that Mr. Thompson's involvement in policy decisions does not establish that Thompson actually determines and carries out policies, in light of the broad responsibilities given Amcell under the management agreement. TDS also claims that Amcell controls Thompson's litigation decisions.

26. *Discussion.* Although Thompson presents evidence that Mr. Thompson has the final say, and thus determines, policy matters,[6] we are troubled by a provision of the Thompson-Amcell Indemnity Agreement, dated December 30, 1987, which raises the possibility of Amcell's dominance. Section 1(c) of the agreement requires Thompson to "cooperate[] fully" with Amcell and gives Amcell "sole control" over the defense or settlement of any demand or claim subject to indemnification. These include claims arising from the Thompson-Amcell management agreement or the "filing by Amcell . . . of any petition, request or other pleading or matter with the FCC." Indemnity Agreement ¶ 1. Although, as Thompson and Amcell point out, this provision relates only to certain litigation, that litigation is potentially highly significant to the Thompson-Amcell relationship.

27. We are concerned that this provision may reflect dominance in some policy matters by Amcell. In this regard, it tends to underscore the difficulty in evaluating, without further inquiry, the credibility of Thompson's claims that Mr. Thompson determines policy through the right to review and approve matters in which Amcell also has extensive involvement.

4. Personnel Responsibilities

28. *Comments.* Thompson and Amcell assert that Amcell's employees operate the Atlantic City system under a valid turnkey management agreement and that it is therefore appropriate for Amcell to handle the hiring, firing, and supervision of these employees. They observe that Thompson selected Amcell as its management company and negotiated the terms of the management agreement. They also observe that Thompson retained an independent FCC counsel and counsel/business adviser as well as Thompson's sole employee, Mr. Thompson. TDS responds that Thompson has no control over Amcell's employees.

29. *Discussion.* Our concern here is similar to our concern discussed in connection with day-to-day operations. Although Thompson's retention of independent counsel provides some evidence of control, the integration of personnel between the Atlantic City and Wilmington systems raises questions as to whether personnel actions will be made on Thompson's -- not Amcell's -- behalf. Given the integration of systems, it is far from clear that Mr. Thompson is "in charge" of personnel matters.

5. Financial Obligations

30. *Comments.* Thompson and Amcell maintain that Thompson has exercised financial responsibility consistent with the retention of control. They assert that Thompson negotiated and is solely liable for the $1.85 million loan used to finance construction of the system and that Amcell has advanced no funds toward system construction or op-

[6] We note in particular evidence that Mr. Thompson exercised control in specific matters. He states that he: (1) rejected a proposal by Amcell to sectorize two new cell sites to be constructed for the Atlantic City system (Declaration of Ellis Thompson, April 1, 1992 at 4); (2) personally, after his contract with Amcell, conducted discussions with TDS and its subsidiary regarding a reseller agreement and the purchase of resale customers (*id.* at 3-4); (3) rejected terms of a lease for the Atlantic City systems retail sales and installation center and negotiated the relevant construction contract (*id.* at 2-3); and (4) disapproved a major agency agreement until Amcell provided a cost analysis justifying the agreement (Declaration of Ellis Thompson, August 20, 1991 at 2-3).

eration. They further assert that all expenses are paid from a separate Thompson bank account to which only Mr. Thompson has unrestricted access, that Thompson must sign all checks for non-recurring expenditures of over $5,000 and all payments to Amcell, and that Amcell bills Thompson for its services and provides regular financial reports to Thompson.

31. TDS contends that Amcell was involved in obtaining the Thompson bank loan and that Amcell makes routine expenditures for the system. TDS claims that Amcell has advanced a large sum of money toward the purchase of the system and has agreed to indemnify Thompson if Thompson should lose its license.

32. *Discussion.* We are concerned that Amcell may have a degree of financial exposure which undercuts the significance of Thompson's formal responsibiity for paying financial obligations. The May 22, 1990 amendment to the Thompson-Amcell Contingent Option Agreement (amendment ¶ 3, ¶ 4, as amended) calls for Amcell to pay Thompson, upon execution of the amendment, $800,000 toward the option price of $6 million. Thompson has made no equivalent out-of-pocket investment in the system. Under the Thompson-Amcell Indemnity Agreement, dated December 30, 1987 (¶ 1), Amcell agreed to reimburse Thompson for litigation expenses and to pay Thompson $750,000 in the event that Thompson's application is denied as a result of execution of the management agreement or as a result of any matter filed by Amcell with the FCC. The September 8, 1990 amendment to the Indemnity Agreement and the Contingent Option Agreement requires Amcell to pay Thompson $1.5 million if Thompson's authorization is revoked as a result of the amendment. These provisions suggest that, although Thompson is formally "in charge" of paying financing obligations, Amcell has actually assumed greater financial obligations than Thompson with respect to the system. Thus, Amcell rather than Thompson may have the true demonstrated financial stake in the system.

33. It also bears noting, in this regard, that there is evidence that Thompson did not negotiate the bank loan used to finance construction of the Atlantic City system "independently of Amcell," as claimed by Thompson. Thompson comments at 9. Although Mr. Thompson negotiated the $1.85 million loan from the Provident Bank used to finance construction of the Atlantic City system, Amcell introduced Mr. Thompson to the bank, and the bank required, as a condition of the loan, that Amcell, with which the bank was familiar, manage the system. *See* Loan Agreement, February 15, 1989 at ¶ 5.1.9; Declaration of Anna E. Hillman (Amcell vice president), May 13, 1991 at 5; Declaration of David A. Lokting (Thompson attorney), May 10, 1991 at 1-3; Declaration of Ellis Thompson, May 16, 1991) at 4. After the provision was questioned, Thompson's lawyer persuaded the bank to modify the condition to permit the substitution of managers with the bank's consent. *Id.* This factor also tends to undermine the significance of Thompon's formally being "in charge" of paying financial obligations.

6. Receipt of Monies and Profits

34. *Comments.* Thompson and Amcell submit that all receipts go into an account controlled by Mr. Thompson and that Thompson receives a pro rata share of all profits. TDS claims the profits actually inure to the benefit of Amcell as the prospective owner of the system under the contingent option agreement. TDS notes that Amcell receives nine percent of gross revenues as a management fee.

35. *Discussion.* The evidence raises questions as to whether Thompson's legal right to receive 50.01 percent of profits reflects the true interests of Thompson and Amcell. In particular, we are concerned by evidence which appears to contradict Thompson's claim that it is "entitled to and *receives* 50.1% of all profits." Thompson Comments at 10. (Emphasis added.) It appears that profits have been distributed only for the purpose of paying taxes and that the system's net income has otherwise been used to pay indebtedness, to reinvest in capital projects, and to maintain cash reserves. Letter from David A. Lokting to Interest Holders (Sept. 15, 1992) at 1-2.

36. The failure to distribute profits raises questions because, at one point, Mr. Thompson represented to the Commission that he was in the process of authorizing a distribution of profits to all interest holders. Declaration of Ellis Thompson, May 16, 1991 at 10. Mr. Thompson ultimately explained that he had cancelled the represented distribution because of pending litigation and uncertainty over the ownership interests in the licensee. Declaration of Ellis Thompson, November 24, 1992 at 3.

37. The circumstances, however, raise the possibility that the failure to distribute profits might be related to Amcell's expectation of imminently acquiring legal ownership of the system. Thompson and Amcell had formally applied for consent to the transfer of the system to Amcell by the time Mr. Thompson gave his explanation for not making the distribution. *See* File No. 08715-TC-01-92. Some circumstances suggest that Amcell's status as a prospective owner of the system, under the Contingent Option Agreement, was always a key factor in the Thompson-Amcell relationship. For example, under the CMS Settlement Agreement, Amcell had the right to disapprove the sale of the system to TDS or any other prospective purchaser. Letter from Sidney Aziz (Amcell) to Leroy Carlson (TDS) (Oct. 15, 1987). Moreover, by the May 22, 1990 amendment to the Contingent Option Agreement (¶ 3), Amcell undertook to make an immediate payment of $800,00 toward the purchase price of the system. Thus, Amcell's evident expectation of acquiring ownership of the system and the failure to distribute any profits to Thompson raises a question as to whether Thompson expected to receive monies and profits from the operation of the system at all.

B. OVERALL SUMMARY

38. We find that the evidence before us discloses a pattern of circumstances which raises a substantial and material question as to whether Thompson permitted Amcell to become a real-party-in-interest in the application. *See Astroline Communications Company Limited Partnership,* 857 F.2d 1556, 1561-62 (D.C. Cir. 1988). We further find that our failure adequately to take into account these circumstances in our prior order rendered our *Intermountain* analysis there incomplete and erroneously led us to conclude that no substantial and material question existed. The relevant circumstances include: (1) Amcell's status as the prospective purchaser of the system; (2) the failure of Thompson to receive profits; (3) Amcell's substantial financial exposure; (4) Amcell's specific assumption of control over litigation related to its management; (5) Amcell's broad management responsibilities

under a long-term agreement; and (6) the consolidation of the facilities and staff of the Atlantic City system and Amcell's operations in adjacent areas.

39. Although no single aspect of Amcell's participation, taken in isolation, necessarily establishes that it has control, the overall pattern could reasonably support a conclusion that, in the expectation of Amcell's acquiring legal control of the system, Thompson permitted Amcell to assume a dominant position with respect to the system's affairs. The elements of the pattern, listed in the preceding paragraph, readily lend themselves to interpretation in that light.

40. We wish to emphasize that the questions raised by this case do not arise merely because the Atlantic City system is being operated pursuant to a turnkey arrangement. We are not suggesting that we expect cellular systems to be run as "mom-and-pop" operations or necessarily to be managed in the manner of broadcast stations. Rather, when we examine the totality of Amcell's involvement here, we find a substantial and material question as to whether Amcell's status as a prospective purchaser of the system with an independent interest in it predominates over its ostensible role as a turnkey manager answerable to Thompson.

41. Moreover, we do not discount the evidence proffered by Thompson tending to indicate that it retains control of the system. However, in view of the evidence as a whole, we find that sufficient doubt has been raised to warrant further inquiry in an evidentiary hearing as to the true relationship between Thompson and Amcell.

42. As we have done in prior cellular radio cases that have been remanded by the court, we will grant Thompson interim authority to continue to operate the Atlantic City system pending the completion of further proceedings. We find that there is a strong public interest in avoiding disruption of service to Ellis Thompson Corporation's customers. Moreover, we find that other applicants for the Atlantic City authorization, who would be subject to random selection procedures, would not be prejudiced by interim operation. *See* 47 C.F.R. § 22.32(g); *La Star Cellular Telephone Co.*, 4 FCC Rcd 3777 (1989), *aff'd*, 899 F.2d 1233 (D.C. Cir. 1990). *See also Metro Mobile CTS, Inc.*, 8 FCC Rcd 8675 (1993), *appeal pending sub nom. JAJ Cellular et. al v. FCC*, No. 94-1021 and consolidated cases (D.C. Cir. Jan.10, 1994); *Portland Cellular Partnership*, 8 FCC Rcd 4146 (1993), *appeal pending sub nom. Saco River Cellular, Inc. et al. v. FCC*, No. 91-1248 and consolidated cases (D.C. Cir. May 23, 1991).

VII. ORDERS

43. ACCORDINGLY, IT IS ORDERED, That, pursuant to the mandate of the Court of Appeals, the authorization issued to Ellis Thompson Corporation to construct and operate the Atlantic City, New Jersey cellular system IS RESCINDED.

44. IT IS FURTHER ORDERED, That pursuant to 47 U.S.C. § 309(e), the application of Ellis Thompson Corporation for facilities in the domestic public radio telecommunications service (File No. 14261-CL-P-134-A-86) IS DESIGNATED FOR HEARING upon the following issue:

> To determine whether American Cellular Network Corporation is a real-party-in-interest in the application of Ellis Thompson Corporation for a cellular radio system on frequency Block A in Atlantic City, New Jersey and, if so, the effect thereof on Ellis Thompson Corporation's qualifications to be a Commission licensee.

45. IT IS FURTHER ORDERED, That the hearing shall be held at a time and place and before an Administrative Law Judge to be specified in a subsequent order.

46. IT IS FURTHER ORDERED, That American Cellular Network Corporation and Telephone and Data Systems, Inc. ARE MADE parties to this proceeding. The applicant and parties to this proceeding may avail themselves of an opportunity to be heard by filing written notices of appearance under 47 C.F.R. § 1.221(c), within 20 days of the mailing of this order by the Secretary of the Commission. The notice and other expedited procedures of 47 C.F.R. § 1.822(b), shall not apply to this proceeding.

47. IT IS FURTHER ORDERED, That pursuant to 47 U.S.C. § 309(e), Telephone and Data Systems, Inc. shall proceed with the initial presentation of evidence with respect to the issue designated above and that the burden of proof with respect to this issue shall be on Ellis Thompson Corporation.

48. IT IS FURTHER ORDERED, That the secretary shall cause a summary of this order to be published in the Federal Register.

49. IT IS FURTHER ORDERED, That Ellis Thompson Corporation IS GRANTED interim authority to operate the Atlantic City, New Jersey cellular system until a new license is granted and has become effective, and, if the licensee is not Ellis Thompson Corporation, any new licensee has given notice to Ellis Thompson Corporation and the Commission that it is ready to commence operation.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

TRANSWORLD COMMUNICATIONS (U.S.A.), INC. — File No. ISP-94-004

Petition to reallocate circuits on the Intersputnik satellite system for the provision of public switched service

ORDER

Adopted: November 15, 1994; Released: November 28, 1994

By the Chief, International Bureau:

1. This proceeding involves the use of the Intersputnik satellite system for the provision of public switched communications services. Transworld Communications (U.S.A.), Inc., noting that many of the Intersputnik circuits we have previously authorized for public switched services[1] have not yet been activated, has filed a petition asking the Commission to revoke and reallocate those circuits to Transworld. IDB Inc., Sprint Communications Company L.P., AT&T Corp., Columbia Communications Corporation, and Direct Net Telecommunications, A Limited Liability Company[2] filed oppositions to or petitions to deny Transworld's petition.[3] Sokol America, Inc. and Transworld filed replies. We grant Transworld's petition in part.

BACKGROUND

2. In 1985, the Commission, after consultation with the Executive Branch, conditionally authorized the establishment of separate satellite systems to provide international public telecommunications services in limited competition with INTELSAT, subject to the restriction that such communications not be interconnected with the public switched network (PSN).[4] At the time, the restriction on interconnection with the PSN was deemed necessary to protect INTELSAT's core revenue base which consisted of switched voice and other services.

3. In 1990, in response to applications from carriers to use the Intersputnik satellite system for switched services, the Executive Branch determined that use of the Intersputnik satellite system should be subject to the same restrictions applicable to U.S. separate satellite systems.[5] These restrictions included the prohibition on interconnection with the PSN, as well as the need for the U.S. to consult with other INTELSAT Parties under Article XIV(d) of the INTELSAT Agreement to ensure technical compatibility and to avoid significant economic harm to INTELSAT.

4. Based in part on determinations by INTELSAT that limited interconnection to the PSN of circuits carried over separate satellite systems would not result in significant economic harm to INTELSAT, the Executive Branch modified the Separate Systems policy to permit up to 1,250 64-kbps equivalent circuits per satellite to be interconnected with the PSN.[6] With respect to Intersputnik, however, only 700 circuits have been "consulted" under Article XIV(d) for U.S.-Russia service. The remaining circuits have been allocated for service between Russia and other locations.

5. Because of the limited number of circuits consulted for U.S.-Russia service, the Commission issued a public notice on August 5, 1991, which established a cut-off date of September 4, 1991 for applications to use Intersputnik satellite circuits. Transworld was not among those applicants filing before the cut-off date and, therefore, was not eligible for consideration. In the *Allocation Order*, the Commission allocated 691 of the 700 available circuits among eleven carriers. The Order required the carriers to file reports detailing the number of circuits activated and specified that the circuits could be revoked if not implemented within ninety days from the release of the order.

6. Transworld asks us to reallocate those circuits not being used. According to Transworld, 533 of the 691 circuits authorized have not been placed into service. Transworld notes that it has had an application pending since April 12, 1993, to acquire 186 Intersputnik circuits. Moreover, Transworld states that it has searched Commission records and has not found circuit activation reports filed by any carriers other than AT&T and IDB, although the *Allocation Order* required each authorized carrier to file these reports.[7] Consequently, Transworld believes it is reasonable to conclude that most carriers are not using their authorized circuits. Transworld argues that fairness

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[1] AT&T, et al., 8 FCC Rcd 2668 (1993) (*Allocation Order*).

[2] Direct Net is the successor in interest of Miralite Communications, Inc., one of the original applicants for the Intersputnik circuits that are the subject of this Petition.

[3] Columbia later withdrew its opposition. Letter from Raul Rodriguez, counsel for Columbia, to Scott Blake Harris, Chief, International Bureau (Oct. 31, 1994).

[4] *Establishment of Satellite Systems Providing International Communications*, 101 FCC 2d 1046 (1985), *on recon.*, 61 R.R.2d 649 (1986), *further recon.*, 1 FCC Rcd 439 (1986) (*Separate Systems*).

[5] Letter from Laurence S. Eagleburger, Deputy Secretary of State, to FCC Chairman Alfred C. Sikes (May 14, 1990).

[6] At its Nineteenth Assembly of Parties Meeting held October 25-28, 1994, INTELSAT determined that the interconnection of up to 8,000 64-kbps equivalent circuits via each separate-system satellite would not cause it significant economic harm. INTELSAT's action may enable us to authorize additional Intersputnik circuits in the future. However, pending before the Commission is a petition filed by Columbia which raises policy issues concerning the expansion of services between the U.S. and Russia and other locations via satellites of the former Soviet Union. *See* Columbia's Petition for Declaratory Ruling, File No. 93-ISP-93-014.

[7] Based on the failure of some carriers to file reports required by the *Allocation Order*, the Commission, in a letter dated May 9, 1994, requested that each applicant explain its failure to file the required reports and explain its failure to activate all of the circuits allocated. The Commission received responses from ten of the eleven authorized carriers.

and equity dictate that it be given the opportunity to implement service over some of the unused Intersputnik capacity.

7. The carriers oppose Transworld's petition. All argue they are using their best efforts to implement the circuits. Sprint cites the difficulties its foreign correspondent has encountered in building an Intersputnik antenna, and in providing earth station capacity and matching facilities in Russia. AT&T states that it has made every effort to activate the circuits as soon as technically feasible but that it has been faced with a variety of technical constraints that have impeded its progress. Direct Net states that, aside from meeting the complex and time-consuming Russian regulatory requirements, it can be quite difficult to obtain and install the necessary customer premises equipment, e.g. state-of-the-art PBX. Sokol states that technical constraints on Russian telecommunications entities have slowed the activation process and that these constraints are largely outside the control of U.S. carriers. Sokol notes that any reallocation of its circuits would undercut its on-going negotiations and would negatively affect its business as a whole. Further, IDB believes that Transworld's request for 186 circuits is excessive in light of IDB's own allocation of 67 circuits, and collectively 154 for its wholly-owned subsidiaries.

8. In its reply, Transworld questions statements by IDB, Direct Net, and Sprint concerning their future plans to activate circuits. Transworld also notes that it has entered into an operating agreement with its duly licensed Russian correspondent, Moscow Teleport, who has agreed to operate up to 120 64-kbps equivalent circuits for PSN services between the U.S. and Russia. Transworld also suggests that the Commission may find a way to accommodate its need for 120 circuits without disturbing the allotments to the responding carriers.

DISCUSSION

9. Upon consideration of Transworld's petition and the responsive pleadings, we grant the petition in part. Transworld's petition requires that we balance two competing considerations: the interests of previously authorized carriers in being given a realistic opportunity to activate their circuits; and the interests of Transworld and other similarly situated carriers in being given the opportunity to activate circuits that have not been placed into service.

10. It appears the carriers have encountered a number of difficulties in procuring Russian regulatory approval and in locating state-of-the-art equipment. Consequently, revocation and reallocation of circuits at this time might well negate the groundwork laid for activating such circuits and prejudice those carriers who are close to either entering an operating agreement or activating circuits. However, these factors cannot justify authorizations remaining effective for an indefinite period of time during which other carriers are denied the opportunity to place these limited number of circuits into service.

11. Although the *Allocation Order* did not identify a specific time limitation on effectiveness of the authorizations, it provided that the circuits could be revoked within 90 days if not placed in service. Thus, the applicants were on notice that they would not be afforded an open-ended opportunity to implement their plans. *See ITT World Communications, Inc. v. F.C.C.*, 595 F.2d 897, 903 (2d Cir. 1979). As the Court noted in *ITT World Communications, Inc. v. F.C.C.*, "there comes a time when an authority unexercised because of inability becomes detrimental to the public interest, since it may discourage other carriers who have the ability from making the investment needed to perform a service; without any benefit to the public." *Id.* at 903. *See also International Relay, Inc.*, 77 F.C.C. 2d 819, 828 (1980); *recon. granted in part*, 82 F.C.C. 2d 41, 45 (1980).[8]

12. Consistent with these principles, we find that the continued inability of the authorized carriers to implement service may be detrimental to the public interest, particularly where other carriers are denied an opportunity to provide service due to the limited number of circuits available. In this case, approximately 18 months have passed since the *Allocation Order* was released, yet many carriers have failed to activate all of the circuits allocated and some carriers have failed to activate any at all. Under these circumstances, we conclude that revocation of at least some of the circuits authorized may be warranted.

13. Despite the difficulties encountered by the authorized carriers in either entering into operating agreements or activating Intersputnik circuits, it is possible that Transworld may be able to activate some of these circuits if given the opportunity. Transworld has procured an operating agreement with Moscow Teleport. Although this agreement does not guarantee Transworld will successfully activate circuits, it provides some evidence of Transworld's progress. In contrast, some of the authorized carriers have yet to enter into the necessary operating agreements.

14. Accordingly, within 45 days from the release date of this order, all carriers authorized to acquire and operate Intersputnik circuits in the *Allocation Order* are required to show cause why their unused Intersputnik circuits should not be revoked and reallocated. In making a determination as to whether such action is warranted, we will consider the carriers' diligence in pursuing an operating agreement and activating the circuits authorized; the precise nature of any technical difficulties or other problems that have delayed the activation of circuits; and whether these difficulties are likely to impede the efforts of other carriers. The parties should fully address each of these considerations in their responses to this Order.

15. Accordingly, IT IS ORDERED that Transworld's petition, File No. I-S-P-94-004 IS GRANTED, in part, to the extent set forth in paragraph 14 *supra*.

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[8] Section 63.05 of the Commission's Rules provides further support for not permitting unexercised Intersputnik authorizations to continue in effect for an indefinite period of time. Section 63.05 specifies that where facilities authorized have not been leased or acquired within 12 months from the date of the Commission's authorization or where all or part of the proposed facilities have not been placed in operation within 36 months after such date, such authorization shall terminate at the end of such 12 or 36 months' period. Section 63.05 provides only the outer boundaries for termination of authorizations and does not preclude the termination of an authorization at an earlier time should such action be required by the public interest.

16. IT IS FURTHER ORDERED that all carriers authorized to establish communications between the U.S. and Russia via the Intersputnik satellite must, within forty-five (45) days from the release date of this order, show cause why their unused Intersputnik circuits should not be revoked.

17. IT IS FURTHER ORDERED that the circuits authorized to any carrier failing to respond to this Order will be automatically revoked without a hearing.

18. IT IS FURTHER ORDERED that this Order is issued pursuant to Section 0.261 of the Commission's Rules and is effective upon release. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the public notice of this order (*see* Section 1.4(b)(2)).

FEDERAL COMMUNICATIONS COMMISSION

Scott Blake Harris
Chief, International Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Star Cable Associates — CUID No. SC0437 (Pelion, SC)
Cost of Service Filing To Support
Cable Programming Service Rate

MEMORANDUM OPINION AND ORDER

Adopted: November 8, 1994; Released: November 9, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On November 24, 1993, Star Cable Associates ("Star Cable") filed a cost of service submission with the Commission in response to a complaint that alleges that Star Cable's cable programming service ("CPS") rate in its Pelion, South Carolina franchise is excessive.[1] On July 13, 1994, Star Cable supplemented and amended its filing as permitted by the Bureau's *May 23 Order*.[2]

2. Star Cable's cost of service filing seeks to establish that its CPS rate of $17.90 per month for the period September 1, 1993, to May 14, 1994, is justified based on Star Cable's cost of providing CPS. Our review of the record indicates that, although not all of the costs in Star Cable's showing are allowable under general cost of service principles, even if we disallow those non-allowable costs, Star Cable's CPS rate in effect for the referenced time period is justified under general cost of service principles.[3]

3. According to information provided by Star Cable in its cost of service submission, its system provides service to approximately 139 basic subscribers and 138 CPS subscribers. Star Cable provides eight channels on its basic tier and 20 channels on its CPS tier.

4. We emphasize that in this review process, pursuant to the 1992 Cable Act, we are analyzing rates for a limited past period, solely for the purpose of determining whether any refund liability has arisen.[4] As discussed below, we are applying general cost of service principles with Commission rules and guidance that were available at the time these filings were made.

II. BACKGROUND

5. On May 3, 1993, the Commission released its *Rate Order* establishing rules to implement the cable television rate regulation provisions of the 1992 Cable Act. In the *Rate Order*, the Commission determined that a benchmark approach should serve as the primary method for regulating basic service and CPS rates. The Commission also concluded that because the benchmark methodology might not produce fully compensatory rates in all cases, it was appropriate to permit operators, as an alternative, to justify rates based on costs, using individual cost of service showings.[5] The cost of service approach was intended to be used only if an operator believed that the maximum rate permitted under the benchmark formula would not enable the operator to recover costs reasonably incurred in providing rate regulated cable services.

6. The Commission found, however, that the record before it at the time of the adoption of the *Rate Order* did not provide sufficient information on which to develop detailed cost of service rules for the cable industry.[6] Therefore, on July 16, 1993, the Commission issued a Notice of Proposed Rulemaking which proposed requirements to govern cost of service showings submitted by cable operators seeking to justify rates higher than those determined under the benchmark approach.[7] The Commission indicated in the *Notice*, as it did in the *Rate Order*, that general cost of service principles would apply to cost of service

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[1] The complaint accepted by the Commission was filed on November 3, 1993. Although not moving to dismiss the CPS complaint, Star Cable argues in its cost of service filing that the underlying complaint is procedurally defective. Star Cable alleges in particular that the complaint lacks a copy of an invoice, references a combined CPS and basic services rate, and references increases pre-dating the effective date of regulation under the 1992 Cable Act. Star Cable's assertions do not persuade us that the complaint is invalid or should be dismissed. In general, we will find valid any complaint that states a claim and provides adequate information to allow us to process the complaint, despite minor flaws or inaccuracies. We believe this approach best implements the mandate of the 1992 Cable Act. Accordingly, we reject Star Cable's arguments that the complaint should be dismissed.

[2] Cable Operators' Rate Justification Filings, Sections 76.945, 76.956 of the Commission's Rules, Order, DA 94-526 (released May 23, 1994) (*"May 23 Order"*); *see also,* Cable Operators' Rate Justification Filings, Order, DA 94-619 (released June 14, 1994). Prior to the deadline for amending or supplementing cost of service filings, Commission staff contacted Star Cable by telephone (with follow-up confirmation letter), to provide the operator with informal guidance as to specific information that staff's preliminary review indicated should be added to or corrected in the operator's pending cost-of-service filing.

[3] This Order does not make any findings or rulings regarding Star Cable's rates for basic service and equipment, or premium services. Regulation of rates for basic service and equipment is generally the responsibility of the local franchising authorities, and premium services are unregulated. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) (*"Rate Order"*) , at 5637. Data for these services were reviewed only to the extent needed for our evaluation of the reasonableness of an operator's CPS rates.

[4] *See* Communications Act of 1934, as amended by the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act"), at § 623(c)(1)(C). The 1992 Cable Act authorizes the Commission to order that the operator refund to subscribers that portion of rates paid after the filing of a valid complaint, that are then found to be unreasonable.

[5] Rate Order, 8 FCC Rcd at 5794-95; *see also,* 47 C.F.R. § 76.922.

[6] *Rate Order,* 8 FCC Rcd at 5798-99.

[7] Implementation of Sections of the Cable Television Con-

filings submitted prior to the adoption of specific rules.[8] Star Cable's cost of service filing under review here was submitted during that pre-adoption time period and covers only the period prior to May 15, 1994. We are analyzing the rates in effect for the period prior to May 15, 1994, as the Commission instructs, under general cost of service principles, not under the rules adopted by the Commission in February 1994.[9]

III. DISCUSSION

7. In analyzing Star Cable's cost of service submission, we considered that the cost of service approach permits rates to be set to allow a company to recover the reasonable costs of providing rate regulated cable services, including an opportunity to earn a fair return on its investment.[10] If we find that a certain rate base or expense element is not supported, is excessive, or is unrelated to providing rate regulated cable service, we can disallow that cost in whole or in part.[11] We have evaluated rate base and expense items to determine whether Star Cable should be permitted to recover those items in its rates. In some cases, we have found costs that are not allowable, and we have made appropriate adjustments. Even with our adjustments and disallowances, however, we find that Star Cable's CPS rate for the period under review has been justified.

8. **Rate Base:** Rate base represents the amount of investment the cable company makes in its facilities to provide service to its customers. Under traditional cost of service principles, it is necessary to determine the allowable rate base in order to calculate the revenue requirement based on the applied rate of return. In analyzing Star Cable's filing, we reviewed the components of Star Cable's rate base to determine the investment upon which Star Cable is entitled to earn a return. For purposes of this review, we made adjustments to the rate base as discussed below.

(a) *Operating Losses:* Star Cable proposes to include in its rate base five years of start-up losses, totaling $47,857. For this review we are allowing operating losses accumulated over the prematurity period as defined by Statement of Financial Accounting Standards No. 51, Financial Reporting by Cable Television Companies ("FAS 51").[12] Under FAS 51, the prematurity phase of a cable television system is presumptively no longer than two years, although it may arguably be longer. Star Cable did not provide any argument that its prematurity period was longer than two years. Accordingly, for purposes of this analysis the recovery of accumulated start-up losses in Star Cable's rate base is limited to two years. We have calculated Star Cable's start-up losses for the first two years as $16,591, net of accumulated amortization. The adjustments are as follows:

	Company	Commission Proposal Allowance	Adjustment
Start-up Losses	$47,857	$19,143	($28,714)
Accum. Amort.- Start-up Losses	($ 9,571)	($ 2,552)	$ 7,019
Net Start-up Allowance/ Adjustment	$38,286	$16,591	$21,695

9. **Rate of Return:** A regulated entity is entitled to the opportunity to earn a fair return on investment.[13] That return should be sufficient to ensure confidence in the financial integrity of the enterprise,[14] but should be balanced with our interest in protecting a company's subscribers. In the *Rate Order* the Commission stated that it would make a case-by-case determination of reasonableness for submissions made before specific cost rules could be adopted.[15] In the rulemaking notice initiating a proceeding to adopt such rules, released several weeks before the submission date of these initial cost of service filings, the Commission discussed its analysis of rate of return generally, and tentatively concluded that an after-tax, overall rate of return in the range of 10-14% would reflect a reasonable balancing of subscriber and cable operator interests.[16] In

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sumer Protection Act of 1992: Rate Regulation, MM Docket No. 93-215, Notice of Proposed Rulemaking, FCC 93-353 (released July 16, 1993), 58 Fed. Reg. 40762 (July 30, 1993) (*"Notice"*) .

[8] *Id.* at 40763; *Rate Order*, 8 FCC Rcd at 5798-99, 5854, n.859.

[9] In February 1994, the Commission adopted an order setting forth specific regulatory requirements to govern cost of service filings to justify rates above levels determined under its benchmark requirements. The new rules apply to rates charged or to be charged after May 15, 1994. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC d 4527 (1994) (*"Cost Order"*).

[10] *See Notice* at 40765:

> Under traditional cost-of-service regulation, rates are set at a level to provide the company with recovery of its costs and a reasonable opportunity to earn a fair return on its invested capital. Under the traditional formulation, the company's revenue requirement is equal to the expenses of providing service and its return on investment.

[11] The Commission made clear that the fact that an operator has incurred costs does not necessarily establish its right to recover those costs from subscribers. *See Rate Order*, 8 FCC Rcd at 5794, n.619. "When electing [to make] a cost of service showing, the cable operator assumes the risk that its rate could be lowered if such action is justified by the cost showing." *Id.* at 5800, para. 272.

[12] FAS 51 establishes standards of financial accounting and reporting for costs, expenses, and revenues applicable to the construction and operation of cable television systems. These standards are considered to be generally accepted accounting principles, and provide guidance as "general cost of service principles," in the absence of specific rules. Under these standards, when a cable system is partially under construction and partially in service (the prematurity period), costs incurred that relate to both current and future operations shall be partially capitalized as start-up costs and partially expensed.

[13] *Notice* at 40769.

[14] *Id.; see also, Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 603 (1944).

[15] *Rate Order*, 8 FCC Rcd at 5795, para. 264.

[16] *See Notice* at 40765. Since the release of the *Notice*, the Commission has adopted a unitary rate of return for cable of 11.25%. *Cost Order*, 9 FCC Rcd at _____, para. 147. The Commission adopted the 11.25% rate of return on an interim basis, based on evidence in the record. However, the *Cost Order* applies to rate justification filings submitted after the effective date of the rules, and not to filings already pending. *Id.* at 4527, para. 5; *see also, Rate Order*, 8 FCC Rcd at 5854, n.859.

the *Notice*, the Commission reached its tentative conclusion of a range of reasonableness from 10-14% based on a summary analysis of the cost of equity and the capital structure of regulated cable services.[17] The *Rate Order* postulated a case-by-case determination of reasonableness regarding the rate of return. As a general approach for evaluation of refund liability from cost of service showings submitted before the effective date of the cost of service rules, we find it appropriate and reasonable to make reference to the range discussed in the *Notice* for our analysis, and to determine the reasonableness of the proffered return in light of that range and of other evidence presented. Star Cable's submission includes an after-tax overall rate of return of 11.25%. This return is reasonable, and we will accept Star Cable's application of an 11.25% rate of return for purposes of our review in this proceeding.

10. **Operating Expenses:** Cable operators may recover in rates their reasonable expenses normally associated with providing rate regulated cable services. Our review of Star Cable's expenses under general cost of service principles results in the adjustments discussed below.

(a) In conjunction with the rate base adjustment to start-up losses, we have adjusted Star Cable's operating expenses. According to generally accepted accounting principles, capitalized start-up losses are to be amortized over the same period used to depreciate the main cable television plant.[18] We believe this is the appropriate standard for the amortization allowance for start-up losses recoverable in regulated charges. Star Cable uses various lives for its headend, trunk and distribution facilities. We have therefore used a weighted average of these lives, an eighteen-year period, for purposes ofamortizing Star Cable's start-up losses.[19] Star Cable's filing includes, on the basis of a ten-year amortization period, $4,786 annual amortization expense for start-up losses, of which $2,900 (60.61%) is allocated to the CPS tier. We have adjusted this amount to allow for two years of accumulated losses. In addition to the adjustment to allow for two years of accumulated losses, we have adjusted the amortization period, as discussed above, from the proposed ten-year period to an eighteen-year period. Amortization of the allowed loss ($19,143) over eighteen years produces in an annual amortization expense of $1,064. Of this expense, $645 is allocable to CPS ($1,064 x .6061). Accordingly, we have disallowed $2,255 ($2,900 - $645) in amortization expense related to the inclusion of excess start-up losses in rate base allocated to the CPS tier.

(b) Star Cable includes operating costs of $1,304 under the category "Other Expenses," and $167 under the category "Other Adjustments." Inclusion of such entries requires a description and explanation of the expenses claimed. Star Cable does not provide the requisite information for either of the two entries, and we have accordingly disallowed these expenses.

11. **Income Tax Allowance:** Star Cable calculates its income tax allowance by simply multiplying its effective tax rate by the equity portion of its return.[20] This methodology is incorrect because it does not allow Star Cable to recover its full provision for income taxes, resulting in a lower earned rate of return. We have adjusted Star Cable's income tax allowance to reflect the use of the proper methodology. Such adjustment increases Star Cable's income tax component from $3,534 to $5,027 (an additional $1,497 to the CPS rate justification).

12. **Star Cable's Proposed Future Rate Increases:** Star Cable indicates in its filing that it does not intend to increase its CPS rate immediately, but that it proposes increases of approximately 4-7% percent per year over the next several years, depending on general inflation and increases in uncontrollable expenses. With regard to the issue of future rate increases, we note that our rate orders and regulations address what are allowable increases and the appropriate procedures for justifying such increases. Once a rate is established through a cost of service showing, the price cap mechanism will govern future increases of the sort Star Cable discusses.[21] The review of Star Cable's rate in this proceeding is to determine the reasonableness of the rate in effect for the period September 1, 1993 to May 14, 1994. Star Cable must file a rate justification for the rates it will charge after May 14, 1994, pursuant to the Commission rules, effective May 15, 1994. Therefore, discussion of Star Cable's proposal regarding future increases is premature.

IV. CONCLUSION

13. Based on our review of Star Cable's cost of service filing and supplemental information, applying general cost of service principles and applicable cost allocation rules, we find that, while Star Cable's cost of service showing overstates its revenue requirement, the CPS rate Star Cable seeks to justify for the period under review, $17.90, is supported by this showing.[22]

14. Accordingly, IT IS ORDERED, pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321, that the CPS rate charged by Star Cable Associates with respect to the above-referenced communities, for the period September 1, 1993, to May 15, 1994, of $17.90, IS JUSTIFIED

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[17] *See Notice* at 40765.

[18] *See* Statement of Financial Accounting Standards No. 51, Financial Reporting by Cable Television Companies, FAS 51, para. 10.

[19] Star Cable depreciates its primary cable plant over a ten-year, twelve-year, and 20-year period. We are using a weighted average of eighteen years as the amortization period.

[20] Star Cable did not compute the tax gross-up rate which requires multiplying the equity portion of the return by the effective tax rate and dividing this amount by (1 - the effective tax rate).

[21] *Cost Order*, 9 FCC Rcd at _____, para. 8.

[22] This finding is based solely on the representations of Star Cable in its cost of service filing. Should information come to our attention that these representations (including representations as to the status of *a la carte* packages or data regarding installations and customer equipment) were materially inaccurate, we reserve the right to take appropriate action. This Order is not to be construed as a finding that we have accepted as correct any specific entry, explanation or argument made by any party to this proceeding not specifically addressed herein (including the operator's Form 393).

under general cost of service principles and applicable allocation rules, and that no refund liability for CPS service during that period will be imposed.[23]

15. IT IS FURTHER ORDERED that the complaint filed against Star Cable Associates regarding its CPS rate for the period September 1, 1993, to May 14, 1994, IS DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[23] The findings in this Order do not in any way prejudge the reasonableness of prices for CPS service after May 14, 1994 under our rate regulations. However, to the extent Star Cable has sought to take advantage of the refund deferral period under the *Second Order on Reconsideration* (Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, 9 FCC Rcd 4119 (1994)), the CPS rate found reasonable herein might also apply from May 15, 1994 until the date on which Star Cable implemented its CPS price under the new regulations.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Cable TV of Georgia, L.P. CUID No. GA0393 (Dahlonega, GA)

Cost of Service Filing to Support
Cable Programming Service Rate

MEMORANDUM OPINION AND ORDER

Adopted: November 8, 1994; Released: November 9, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On February 14, 1994, Cable TV of Georgia, L.P. ("Cable TV of Georgia") filed a cost of service showing with the Commission in response to a complaint regarding its cable programming service ("CPS") rate in its Dahlonega franchise and requested confidentiality in respect to the cost of service showing.[1] On July 14, 1994, Cable TV of Georgia supplemented and amended its filing, as permitted by the Bureau's *May 23 Order*.[2] On September 12, 1994, in response to Commission inquiry, Cable TV of Georgia submitted additional amended data.

2. Cable TV of Georgia's cost of service filing seeks to establish that its CPS rate of $13.75 per month for the period of September 1, 1993 to May 14, 1993, is justified based on its cost of providing CPS. Our review of the record indicates that, although not all of the costs in Cable TV of Georgia's showing are allowable under general cost of service principles, even if we disallow those non-allowable costs, Cable TV of Georgia's CPS rate in effect for the referenced time period is justified under general cost of service principles.[3]

3. According to information provided by Cable TV of Georgia in its cost of service submission, its system provides service to approximately 728 basic subscribers and 690 CPS subscribers. Cable TV of Georgia provides fourteen channels on its basic tier and eighteen channels on its CPS tier.

4. We emphasize that in this review process, pursuant to the 1992 Cable Act, we are analyzing rates for a limited past period, solely for the purpose of determining whether any refund liability has arisen.[4] As discussed below, we are applying general cost of service principles with Commission rules and guidance that were available at the time these filings were made.

II. BACKGROUND

5. On May 3, 1993, the Commission released its *Rate Order* establishing rules to implement the cable television rate regulation provisions of the 1992 Cable Act. In the *Rate Order*, the Commission determined that a benchmark and price cap approach should serve as the primary method for regulating basic service and CPS rates. The Commission also concluded that because the benchmark methodology might not produce fully compensatory rates in all cases, it was appropriate to permit operators, as an alternative, to justify rates based on costs, using individual cost of service showings.[5] The cost of service approach was intended to be used only if an operator believed that the maximum rate permitted under the benchmark formula would not enable the operator to recover costs reasonably incurred in providing rate regulated cable services.

6. The Commission found, however, that the record before it at the time of the adoption of the *Rate Order* did not provide sufficient information on which to develop detailed cost of service rules for the cable industry.[6] Therefore, on July 16, 1993, the Commission issued a Notice of Proposed Rulemaking which proposed requirements to govern cost of service showings submitted by cable operators seeking to justify rates higher than those determined under the benchmark approach.[7] The Commission indicated in the *Notice*, as it did in the *Rate Order*, that general cost of service principles would apply to cost of service

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[1] The complaint accepted by the Commission was filed on January 21, 1994. The complainant filed a complaint against Cable TV of Georgia-Dahlonega listing GA0393 as the CUID number. The response filed by Cable TV of Georgia lists the CUID number as GA0601; research by Bureau staff revealed that the correct CUID number is GA0393.

[2] Cable Operator's Rate Justification Filings, Sections 76.945, 76.956 of the Commission's Rules, Order, DA 94-526 (released May 23, 1994) (*"May 23 Order"*); *see also*, Cable Operators' Rate Justification Filings, Order, DA 94-619 (released June 14, 1994). Prior to the deadline for amending or supplementing cost of service filings, Commission staff contacted Cable TV of Georgia by telephone (with follow-up confirmation letter), to provide the operator with informal guidance as to specific information that staff's preliminary review indicated should be added to or corrected in the operator's pending cost-of-service filing.

[3] This Order does not make any findings or rulings regarding Cable TV of Georgia's rates for basic service and equipment, or premium services. Regulation of rates for basic service and equipment is generally the responsibility of the local franchising authorities, and premium services are unregulated. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) (*"Rate Order"*), at 5637. Data for these services were reviewed only to the extent needed for our evaluation of the reasonableness of an operator's CPS rates.

[4] *See* Communications Act of 1934, as amended by the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act"), at § 623(c)(1)(C). The 1992 Cable Act authorizes the Commission to order that the operator refund to subscribers that portion of rates paid after the filing of a valid complaint, that are then found to be unreasonable.

[5] *Rate Order*, 8 FCC Rcd at 5794-95; *see also*, 47 C.F.R. § 76.922.

[6] *Rate Order*, 8 FCC Rcd at 5798-99.

[7] Implementation of Sections of the Cable Television Consumer Protection Act of 1992: Rate Regulation, MM Docket No. 93-215, Notice of Proposed Rulemaking, FCC 93-353 (released July 16, 1993), 58 Fed. Reg. 40762 (July 30, 1993) (*"Notice"*).

filings submitted prior to the adoption of specific rules.[8] Cable TV of Georgia's cost of service filing under review here was submitted during that pre-adoption time period and covers only the period prior to May 15, 1994. We are analyzing the rates in effect for the period prior to May 15, 1994, as the Commission instructs, under general cost of service principles, not under the rules adopted by the Commission in February 1994.[9]

III. DISCUSSION

7. In analyzing Cable TV of Georgia's cost of service submission, we considered that the cost of service approach permits rates to be set to allow a company to recover the reasonable costs of providing rate regulated cable services, including an opportunity to earn a fair return on its investment.[10] If we find that a certain rate base or expense element is not supported, is excessive, or is unrelated to providing rate regulated cable service, we can disallow that cost in whole or in part.[11] We have evaluated rate base and expense items to determine whether Cable TV of Georgia should be permitted to recover those items in its rates. In some cases, we have found costs that are not allowable, and we have made appropriate adjustments. Even with our adjustments and disallowances, however, we find that Cable TV of Georgia's CPS rate for the period under review has been justified.

8. **Confidentiality Request:** In the cover letter to its July 13, 1994 submission, Cable TV of Georgia requests confidential treatment of the cost of service submission on the grounds that it consists of commercial and financial information which is not customarily released to the public. Section 0.459 of the Commission's rules provides that a party submitting information to the Commission may request confidentiality with respect to specific portions of the material.[12] However, the party must show by a preponderance of the evidence that nondisclosure is consistent with the provisions of the Freedom of Information Act ("FOIA").[13] Exemption 4 of the FOIA authorizes the Commission to withhold from public disclosure trade secrets as well as confidential commercial or financial information.[14]

(a) Exemption 4 of the FOIA covers two broad categories: (1) trade secrets; and (2) information which is (a) commercial or financial, and (b) obtained from a person, and (c) privileged or confidential.[15] The confidential or privileged criterion is satisfied if either (1) disclosure of the information is likely to impair the government's ability to obtain necessary information in the future or (2) disclosure is likely to cause substantial harm to the competitive position of the person from whom the information was obtained.[16]

(b) In this case, Cable TV of Georgia does not claim that the information constitutes a trade secret. Cable TV of Georgia asserts that the information is commercial or financial and thus is required to show that the information is privileged or confidential. With respect to the "impairment" prong of the "confidential or privileged" criterion, we conclude that the FCC's information-gathering abilities in this context would not be impaired. The 1992 Cable Act specifically requires cable operators to file with the Commission or franchising authorities such financial information as is necessary to administer and enforce cable service rate regulation.[17] Therefore, the pivotal question is whether, pursuant to the second prong of the test, disclosure of the material is likely to cause substantial competitive harm to Cable TV of Georgia.

(c) The Commission has said that "While an elaborate economic analysis need not be made to establish the likelihood of substantial competitive injury, 'conclusory and generalized allegations' cannot support nondisclosure."[18] In this case, Cable TV of Georgia has baldly asserted that the submission consists of commercial and financial information which is not customarily released to the public. However, Cable TV of Georgia has made no allegations concerning the likelihood of competitive harm which would result if the materials were made available to the public.

(d) We conclude that Cable TV of Georgia has failed to demonstrate any likelihood of competitive injury resulting from disclosure of the cost of service submission for the City of Dahlonega. Furthermore,

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[8] *Id.* at 40763; *Rate Order*, 8 FCC Rcd at 5798-99, 5854, n.859.

[9] In February 1994, the Commission adopted an order setting forth specific regulatory requirements to govern cost of service filings to justify rates above levels determined under its benchmark requirements. The new rules apply to rates charged or to be charged after May 15, 1994. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd 4527 (1994) (*"Cost Order"*).

[10] *See Notice* at 40765:

> Under traditional cost-of-service regulation, rates are set at a level to provide the company with recovery of its costs and a reasonable opportunity to earn a fair return on its invested capital. Under the traditional formulation, the company's revenue requirement is equal to the expenses of providing service and its return on investment.

[11] The Commission made clear that the fact that an operator has incurred costs does not necessarily establish its right to recover those costs from subscribers. *See Rate Order*, 8 FCC Rcd at 5794, n.619. "When electing [to make] a cost of service showing, the cable operator assumes the risk that its rate could be lowered if such action is justified by the cost showing." *Id.* at 5800, para. 272.

[12] 47 C.F.R. § 0.459.

[13] 47 C.F.R. § 0.459(d), *citing* 5 U.S.C. § 552.

[14] *See* 5 U.S.C. § 552(b)(4) (1993).

[15] *Id.*

[16] *See Nat'l Parks and Conservation Ass'n v. Morton*, 498 F.2d 765, 770 (D.C. Cir. 1974). The Court of Appeals later reaffirmed this test, but confined it to those cases involving information that persons were *required* to provide the government. *Critical Mass Energy Project v. NRC*, 975 F.2d 871 (D.C. Cir. 1992). In cases involving financial or commercial information that was supplied *voluntarily* to the government, Exemption 4 applies if the information is of a kind that the provider would not customarily release to the public. *Id.* at 879-880.

[17] *See* 1992 Cable Act at § 623(g).

[18] National Exchange Carrier Ass'n. Inc. (Release of Common Line Pool Audit Report), 5 FCC Rcd 7184 (1990) (*quoting Nat'l Parks and Conservation Ass'n v. Kleppe*, 547 F.2d 673, 680-81 (D.C. Cir. 1976).

there is a compelling public interest supporting disclosure of the cost of service submission.[19] Subscribers have a vital interest in the conduct and outcome of cable rate proceedings which are based upon these materials. For all of these reasons, we find that Cable TV of Georgia has failed to make a showing adequate to warrant the granting of its request for confidentiality.

9. **Rate Base:** Rate base represents the amount of investment the cable company makes in its facilities to provide service to its customers. Under traditional cost of service principles, it is necessary to determine the allowable rate base in order to calculate the revenue requirement based on the applied rate of return. In analyzing Cable TV of Georgia's filing, we have reviewed the components of Cable TV of Georgia's rate base to determine the investment upon which Cable TV of Georgia is entitled to earn a return. Pursuant to our review, we are adjusting Cable TV of Georgia's rate base as discussed below.

(a) *Operating Losses:* Cable TV of Georgia proposes to include in its rate base five years of start-up losses, totaling $224,000. For this review we are allowing operating losses accumulated over the prematurity period as defined by Statement of Financial Accounting Standards No. 51, Financial Reporting by Cable Television Companies ("FAS 51").[20] Under FAS 51, the prematurity phase of a cable television system is presumptively no longer than two years, although it may arguably be longer. Cable TV of Georgia did not provide any argument that its prematurity period was longer than two years. Accordingly, for purposes of this analysis the recovery of accumulated start-up losses in Cable TV of Georgia's rate base is limited to two years. We have calculated Cable TV of Georgia's start-up losses for the first two years as $163,000. Consistent with Cable TV of Georgia's loss computation, we have reduced this amount for income taxes, resulting in capitalized start-up losses of $101,000.

(b) *Allocation:* Cable TV of Georgia provides an allocation key that shows how asset values at the system level are allocated to the franchise level. Cable TV of Georgia then uses various allocators to assign costs to each tier. The Commission's rules in effect at the time of Cable TV of Georgia's filing clearly specify that inter-tier allocations are to be made based on the ratio of channels on each tier to the total number of channels offered.[21] For Cable TV of Georgia, the appropriate channel ratios are 37.84% (14 channels of 37 total) for Basic, and 48.65% (18 channels of 37 total) for CPS. The cumulative effect of our adjustments, including those to allowable losses and rate base allocations, on Cable TV of Georgia's CPS-allocated portion of rate base produces a disallowance of $106,290.

10. **Rate of Return:** A regulated entity is entitled to the opportunity to earn a fair return on investment.[22] That return should be sufficient to ensure confidence in the financial integrity of the enterprise,[23] but should be balanced against our interest in protecting a company's subscribers from paying excessive rates. In the *Rate Order* the Commission stated that it would make a case-by-case determination of reasonableness for submissions made before specific cost rules could be adopted.[24] In the rulemaking notice initiating a proceeding to adopt such rules, released several weeks before the submission date of these initial cost of service filings, the Commission discussed its analysis of rate of return generally, and tentatively concluded that an after-tax, overall rate of return in the range of 10-14% would reflect a reasonable balancing of subscriber and cable operator interests.[25] In the *Notice*, the Commission reached itstentative conclusion of a range of reasonableness from 10-14% based on a summary analysis of the cost of equity and the capital structure of regulated cable services.[26] The *Rate Order* postulated a case-by-case determination of reasonableness regarding the rate of return. As a general approach for evaluation of refund liability from cost of service showings submitted before the effective date of the cost of service rules, we find it appropriate and reasonable to make reference to the range discussed in the *Notice* for our analysis, and to determine the reasonableness of the proffered return in light of that range and of other evidence presented. Cable TV of Georgia uses a rate of return of 11.25%, which we find reasonable. Thus, we have made no adjustments in this regard.

11. **Operating Expenses:** Cable operators may recover in rates their reasonable expenses normally associated with providing rate regulated cable service. Our review of Cable TV of Georgia's expense results in the adjustments discussed below. However, even with these adjustments, Cable TV of Georgia's CPS rate for the period in question is justified.

(a) The problems related to Cable TV of Georgia's rate base allocation calculations also apply to its allocation of operating expenses. In conjunction with

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[19] *See, e.g.,* TKR Cable Company of Ramapo, Order, DA 94-759 (released July 7, 1994) (presence of compelling public interest supported disclosure of financial data in cable ratemaking matter).

[20] FAS 51 establishes standards of financial accounting and reporting for costs, expenses, and revenues applicable to the construction and operation of cable television systems. These standards are considered to be generally accepted accounting principles, and provide guidance as "general cost of service principles," in the absence of specific rules. Under these standards, when a cable system is partially under construction and partially in service (the prematurity period), costs incurred that relate to both current and future operations shall be partially capitalized as start-up costs and partially expensed.

[21] *See Rate Order,* 8 FCC Rcd at 5976.

[22] *Notice* at 40769.

[23] *Id.; see also, Federal Power Commission v. Hope Natural Gas Company,* 320 U.S. 591, 603 (1944).

[24] *Rate Order,* 8 FCC Rcd at 5795, para. 264.

[25] *See Notice* at 40765. Since the release of the *Notice,* the Commission has adopted a unitary rate of return for cable of 11.25%. *Cost Order,* 9 FCC Rcd at _____, para. 147. The Commission adopted the 11.25% rate of return on an interim basis, based on evidence in the record. However, the *Cost Order* applies to rate justification filings submitted after the effective date of the rules, and not to filings already pending. *Id.* at 4527, para. 5; *see also, Rate Order,* 8 FCC Rcd at 5854, n.859.

[26] *See Notice* at 40765.

our reduction in start-up losses, we have reduced Cable TV of Georgia's amortization expense for start-up losses. Additionally, Cable TV of Georgia uses various allocators for expenses allocable to basic and CPS tiers rather than channel ratios; again, we have recomputed the allocations using channel ratios for all expenses allocable to basic and CPS tiers. The effect of this adjustment to the CPS portion of Cable TV of Georgia's operations produces a disallowance of $3,324.

(b) In a memorandum accompanying the cost of service submission, Cable TV of Georgia describes a transaction whereby facilities are rented under an operating lease from a partnership in which Cable TV of Georgia's general partner holds a controlling interest. The return on investment realized by the partnership (the lessor) under this transaction is unclear, although the partnership's net income represented 34% of annual rents. Given the general partner's controlling interest in both the lessor and lessee entities, we are concerned that excess rents may have been paid to the lessor. Subscribers should not bear the burden of costs higher than what would be incurred in an arm's length transaction. However, we do not have a record upon which to determine whether the rental amount Cable TV of Georgia paid was reasonable. Nevertheless, an exclusion of any or all of the net rental income received by the partnership would not invalidate Cable TV of Georgia's CPS rate for the period in question under this filing.

V. CONCLUSION

12. Based on our review of Cable TV of Georgia's cost of service filing and supplemental information, applying general cost of service principles and applicable cost allocation rules, we find that, while Cable TV of Georgia's cost of service showing overstates its revenue requirement, the CPS rate Cable TV of Georgia seeks to justify for the period under review, $13.75, is supported by this showing.[27]

13. Accordingly, IT IS ORDERED, pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321, that the CPS rate charged by Cable TV of Georgia, L.P. with respect to the above-referenced CUID number, for the period September 1, 1993 to May 15, 1994, of $13.75, IS JUSTIFIED under general cost of service principles, and no refund liability for CPS services during that period will be imposed.[28]

14. IT IS FURTHER ORDERED, pursuant to Section 4(i) of the Communications Act of 1934, as amended, 47 U.S.C. § 154(i), that the request of Cable TV of Georgia, L.P. for confidentiality of its cost of service showing for cable programming service rates in the City of Dahlonega IS DENIED.

15. IT IS FURTHER ORDERED that the complaint filed against CableTV of Georgia, L.P. regarding its CPS rate for the period September 1, 1993, to May 14, 1994, IS DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[27] This finding is based solely on the representations of Cable TV of Georgia in its cost of service filing. Should information come to our attention that these representations (including representations as to the status of *a la carte* packages or data regarding installations and customer equipment) were materially inaccurate, we reserve the right to take appropriate action. This Order is not to be construed as a finding that we have accepted as correct any specific entry, explanation or argument made by any party to this proceeding not specifically addressed herein (including the operator's Form 393).

[28] The findings in this Order do not in any way prejudge the reasonableness of prices for CPS service after May 14, 1994 under our rate regulations. However, to the extent Cable TV of Georgia has sought to take advantage of the refund deferral period under the *Second Order on Reconsideration* (Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, 9 FCC Rcd 4119 (1994)), the CPS rate found reasonable herein might also apply from May 15, 1994 until the date on which Cable TV of Georgia implemented its CPS price under the new regulations.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Communications & Cable of Chicago, Inc.	CUID Nos. IL1104 (Chicago, IL) IL1105 (Chicago, IL)
South Chicago Cable, Inc.	

Cost of Service Filing To Support
Cable Programming Service Rate

MEMORANDUM OPINION AND ORDER

Adopted: November 8, 1994; Released: November 9, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On June 29, 1994, Communications & Cable of Chicago, Inc. ("CCCI"), serving Franchise Area 1 of the City of Chicago, and South Chicago Cable, Inc. ("SCCI"), serving Franchise Area 5 of the City of Chicago (together, "Chicago Cable"),[1] each filed a cost of service showing with the Commission in response to complaints regarding the cable programming service ("CPS") rate in effect in their respective franchise areas.[2] On September 2, 1994, both CCCI and SCCI filed amended cost of service data for their franchise areas.[3] Our review examines the June 29, 1994, cost of service filing and the amended filing of September 2, 1994, for both CCCI and SCCI.

2. Chicago Cable's cost of service filing seeks to establish that its CPS rate of $11.29 per month for the period September 1, 1993, to May 14, 1994, is justified based on its cost of providing CPS. Our review of the record indicates that, although not all of the costs in Chicago Cable's showing are allowable under general cost of service principles, even if we disallow those non-allowable costs, Chicago Cable's CPS rate in effect for the referenced time period is justified under general cost of service principles and applicable allocation rules.[4]

3. According to information provided by Chicago Cable in its cost of service submission, Chicago Cable provides service to approximately 195,703 basic subscribers and 189,526 CPS subscribers. Chicago Cable provides 31 channels on its basic tier and 26 channels on its CPS tier. Pursuant to our rules, cable operators are required to present cost of service showings at the franchise level.[5] Chicago Cable has submitted identical system-wide cost of service analyses to support its CPS rates in Franchise Areas 1 and 5. Chicago Cable maintains that it is appropriate and efficient to present its cost of service showings at the system level because Chicago Cable serves both franchise areas through the same cable system, charges the same prices for all cable services and associated equipment in both areas, offers the same channel line-ups in both areas, is regulated by the same franchising authority and pays the same franchise fees in both areas. Our review of the record indicates that information provided in Chicago Cable's submissions support these claims. Because there are no significant distinctions between Chicago Cable's services and rates in these two areas, we will permit the single showing.[6]

4. We emphasize that in this review process, pursuant to the 1992 Cable Act, we are analyzing rates for a limited past period, solely for the purpose of determining whether any refund liability has arisen.[7] As discussed below, we are applying general cost of service principles with Commission rules and guidance that were available at the time these filings were made.

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[1] These two companies are affiliated companies and both do business in their respective franchise areas under the name "Chicago Cable TV." A third affiliated company, LaSalle Telecommunications, Inc., provides cable television service to Franchise Area 4 of the City of Chicago. Chicago Cable TV provides cable service to a combined total of approximately 147,017 households in the two franchise areas.

[2] SCCI states that its cost of service filing for Franchise Area 5 is in response to one complaint, dated April 8, 1994, which was filed by the Cable Administrator for the City of Chicago. Our records indicate that three other valid complaints were filed with respect to CPS rates in Franchise Area 5. CCCI also states that its cost of service filing for Franchise Area 1 is in response to one complaint, dated April 8, 1994, which was filed by the Cable Administrator for the City of Chicago. Again, our records indicate that other valid complaints were filed with respect to Chicago Cable's CPS rates in Franchise Area 1.

[3] On September 2, 1994, both operators submitted amendments to their filings to correct certain erroneous calculations. These amendments were not made in response to Commission requests. Although we will consider these late-filed amendments for purposes of this review, we note that these operators have been consistently late with respect to our filing deadlines. To continue filing accepting updates and amendments outside of our established deadlines undermines our review process, and we will not routinely permit such practices. Any operator making such a late filing runs the risk of its not being considered in our determinations. It is incumbent upon all operators to ensure that their filings are accurate and final when submitted to the Commission for filing.

[4] This Order does not make any findings or rulings regarding Chicago Cable's rates for basic service and equipment, or premium services. Regulation of rates for basic service and equipment are generally the responsibility of the local franchising authorities, and premium services are unregulated. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) (*"Rate Order"*) , at 5637. Data for these services were reviewed only to the extent needed for our evaluation of the reasonableness of an operator's CPS rates .

[5] *See Rate Order*, 8 FCC Rcd at 5977, para. 559; 47 C.F.R. § 76.924(e)(1).v

[6] Chicago Cable provides information at three organizational levels -- corporate (Tele-Communications, Inc.), division (TCI Great Lakes, Inc.), and system (South Chicago Cable, Inc. and subsidiaries) -- in order to establish the allocation of higher level costs to the Franchise Areas 1 and 5. Our examination of Chicago Cable's cost of service showing encompasses a review of Chicago Cable's costs at all three levels.

[7] *See* Communications Act of 1934, as amended by the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act"), at § 623(c)(1)(C). The 1992 Cable Act authorizes the Commission

II. BACKGROUND

5. On May 3, 1993, the Commission released its *Rate Order* establishing rules to implement the cable television rate regulation provisions of the 1992 Cable Act. In the *Rate Order,* the Commission determined that a benchmark and price cap approach should serve as the primary method for regulating basic service and CPS rates. The Commission also concluded that because the benchmark methodology might not produce fully compensatory rates in all cases, it was appropriate to permit operators, as an alternative, to justify rates based on costs, using individual cost of service showings.[8] The cost of service approach was intended to be used only if an operator believed that the maximum rate permitted under the benchmark formula would not enable the operator to recover costs reasonably incurred in providing rate regulated cable services.

6. The Commission found, however, that the record before it at the time of the adoption of the *Rate Order* did not provide sufficient information on which to develop detailed cost of service rules for the cable industry.[9] Therefore, on July 16, 1993, the Commission issued a Notice of Proposed Rulemaking which proposed requirements to govern cost of service showings submitted by cable operators seeking to justify rates higher than those determined under the benchmark approach.[10] The Commission indicated in the *Notice,* as it did in the *Rate Order,* that general cost of service principles would apply to cost of service filings submitted prior to the adoption of specific rules.[11] Chicago Cable's cost of service filing under review here was submitted during that pre-adoption time period and covers only the period prior to May 15, 1994. We are analyzing the rates in effect for the period prior to May 15, 1994, as the Commission instructs, under general cost of service principles, not under the rules adopted by the Commission in February 1994.[12]

III. DISCUSSION

7. In analyzing Chicago Cable's cost of service submission, we considered that the cost of service approach permits rates to be set to allow a company to recover the reasonable costs of providing rate regulated cable services, including an opportunity to earn a fair return on its investment.[13] If we find that a certain rate base or expense element is not supported, is excessive, or is unrelated to providing rate regulated cable service, we can disallow that cost in whole or in part.[14] We have evaluated rate base and expense items to determine whether Chicago Cable should be permitted to recover those items in its rates. In some cases, we have found costs that are not allowable, and we have made appropriate adjustments. Even with our adjustments and disallowances, however, we find that Chicago Cable's CPS rate for the period under review has been justified.

8. **Late-filed Responses:** Chicago Cable moves to have the Commission accept its late-filed responses. Chicago Cable's filings reference only complaints (one for each franchise area) filed by the Cable Administrator of the City of Chicago, and its motions to accept late-filed responses address only the filing deadlines related to these complaints. These complaints were served on the operator on April 8, 1994, thus establishing May 7, 1994, as Chicago Cable's filing deadline for responding to those complaints.[15] With respect to the additional pending complaints not referenced by Chicago Cable, Chicago Cable was required to file responses at least as early as November 22, 1993, for Franchise Area 1, and January 17, 1994, for Franchise Area 5. Chicago Cable filed its cost of service showings (in response to the Cable Administrator's re-filed complaints) on June 29, 1994. Chicago Cable later amended these showings on September 2, 1994.

(a) Chicago Cable maintains that it overlooked the filing deadline due to confusion caused by the return of the initial complaints filed by the Cable Administrator. Chicago Cable asserts that the Cable Administrator's unsuccessful attempt to file complaints for three of the franchise areas that Chicago Cable serves, while at the same time it was seeking certification to regulate only two of the three franchise areas, caused Chicago Cable to overlook the 30-day deadline for a response to the most recent complaint. Chicago Cable also relies on the *May 23 Order* which created a window during which cable operators might correct deficiencies in filings related to CPS rate

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to order that the operator refund to subscribers that portion of rates paid after the filing of a valid complaint, that are then found to be unreasonable.

[8] *Rate Order* , 8 FCC Rcd at 5794-95; *see also,* 47 C.F.R. § 76.922.

[9] *Rate Order,* 8 FCC Rcd at 5798-99.

[10] Implementation of Sections of the Cable Television Consumer Protection Act of 1992: Rate Regulation, MM Docket No. 93-215, Notice of Proposed Rulemaking, FCC 93-353 (released July 16, 1993), 58 Fed. Reg. 40762 (July 30, 1993) *("Notice").*

[11] *Id.* at 40763; *Rate Order,* 8 FCC Rcd at 5798-99, 5854, n.859.n

[12] In February 1994, the Commission adopted an order setting forth specific regulatory requirements to govern cost of service filings to justify rates above levels determined under its benchmark requirements. The new rules apply to rates charged or to be charged after May 15, 1994. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, (Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd 4527 (1994) *("Cost Order").*

[13] *See Notice* at 40765: Under traditional cost-of-service regulation, rates are set at a level to provide the company with recovery of its costs and a reasonable opportunity to earn a fair return on its invested capital. Under the traditional formulation, the company's revenue requirement is equal to the expenses of providing service and its return on investment.

[14] The Commission made clear that the fact that an operator has incurred costs does not necessarily establish its right to recover those costs from subscribers. *See Rate Order,* 8 FCC Rcd at 5794, n.619. "When electing [to make] a cost of service showing, the cable operator assumes the risk that its rate could be lowered if such action is justified by the cost showing." *Id.* at 5800, para. 272.

[15] The complaints were initially filed with the Commission on February 28, 1994. On March 16, 1994, the Commission returned both complaints to the complainant as defective. On April 8, 1994, the complainant timely re-filed and served the complaints. Pursuant to 47 C.F.R. § 79.956, Chicago Cable was required to respond to the complaints within 30 days, thus establishing May 7, 1994, as Chicago Cable's filing deadline with respect to those complaints.

complaints.[16] Chicago Cable maintains that among the "common deficiencies" for which the *May 23 Order* permits correction is the failure to make a rate justification within the 30-day period provided for in 47 C.F.R. § 76.956. Chicago Cable also argues that neither the Commission nor any interested party will be prejudiced by the timing of Chicago Cable's rate justification submissions.

(b) In failing to respond to complaints served since October 12, 1993 (for CPS rates in effect for Franchise Area 5) and December 17, 1993 (for CPS rates in effect for Franchise Area 1), Chicago Cable was in default of the Commission's rules. The window of opportunity provided by the *May 23, 1994 Order* addresses situations where a cable operator failed to file a rate justification based on its decision to request dismissal of the rate complaint or its decision to file a cost of service showing. In this case, Chicago Cable did not respond in any manner to complaints filed as long ago as October 12, 1993. Under our rules, a cable operator that is deemed to be in default may be subject to a finding that its rates are unreasonable and appropriate relief may be mandated by the Commission.

(c) Our decision to review Chicago Cable's rate justification does not condone either Chicago Cable's failure to observe the Commission's filing requirements with respect to the two complaints it references, nor its failure to acknowledge and respond to the numerous other complaints filed against it. We reiterate that, in the future, in order to preserve the integrity of our cable rate regulation process, we will impose forfeitures and other sanctions as appropriate for violations of our rules.

9. **Rate Base:** Rate base represents the amount of investment the cable company makes in its facilities to provide service to its customers. Under traditional cost of service principles, it is necessary to determine the allowable rate base in order to calculate the revenue requirement based on the applied rate of return. In analyzing Chicago Cable's filing, we reviewed the components of Chicago Cable's rate base to determine the investment upon which it is entitled to earn a return. For purposes of this review, we made adjustments to the rate base as discussed below.

(a) At the system level, Chicago Cable failed to explain $300,000 of "Other Intangibles." We have disallowed the $300,000 claimed assets, as well as the associated "Amortization Expense," because there is no description or explanation of these entries.

(b) Chicago Cable includes $13.1 million in plant under construction in rate base. It states that the associated upgrade will be completed by the end of 1994. Under general cost of service principles, allowable costs in rate base are associated with plant that is used and useful. Since there is no indication that this plant was used and useful at the time of filing, for purposes of our analysis we have removed the amount reported as plant under construction from the rate base and made appropriate adjustments to the CPS revenue requirement.

(c) In assessing allowable operating losses associated with the start up phase, we looked to the Statement of Financial Accounting Standards No. 51 ("FAS 51") which allows for capitalization of specified start up losses accumulated over a period presumed to be no longer than two years (the prematurity period).[17] Chicago Cable included in its accumulated depreciation account a contra amount (*i.e.*, a debit) of $4,761,000. It states that this amount represents start up losses for two years. Because the inclusion of this amount as a debit to accumulated depreciation has the same effect on the rate base as recording the amount, consistent with FAS 51, as an intangible asset, we have allowed for the inclusion of losses based on this amount--though we do not agree with the accounting methodology applied.[18] Because it does not appear from the presentation that amortization has been applied to the recorded amount since the end of the presumed-two-year prematurity period, we have adjusted the amount claimed to account for the amortization that should have been taken since 1988. According to FAS 51, capitalized start-up losses are to be amortized over the same period used to depreciate the main cable television plant. Chicago Cable uses a useful life of fifteen years for its headend, trunk and distribution facilities. Therefore, we used a fifteen-year period for purposes of amortizing Chicago Cable's start-up losses. We have, therefore, disallowed $1,900,000 from the rate base, representing the amount of amortization that should have been taken over previous years.

10. **Rate of Return:** A regulated entity is entitled the opportunity to earn a return on investment.[19] That return should be sufficient to ensure confidence in the financial integrity of the enterprise,[20] but should be balanced with our interest in protecting a company's subscribers. In the *Rate Order* the Commission stated that it would make a case-by-case determination of reasonableness for submissions made before specific cost rules could be adopted. [21] In the rulemaking notice initiating a proceeding to adopt such rules, released several weeks before the submission date of these initial cost of service filings, the Commission discussed its analysis of rate of return generally, and tentatively concluded that an after-tax, overall rate of return in

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[16] Cable Operators' Rate Justification Filings, Sections 76.945, 76.956 of the Commission's Rules, Order, DA 94-526 (released May 23, 1994) (*"May 23 Order"*); *see also*, Cable Operators' Rate Justification Filings, Order, DA 94-619 (released June 14, 1994).

[17] Statement of Financial Accounting Standards No. 51, Financial Reporting by Cable Television Companies, para. 10. Standards established by FAS 51 are considered to be generally accepted accounting principles.

[18] The amount should not, in our opinion, be shown in accumulated depreciation but as a separate intangible asset. Further, the recorded amount should be amortized, and the related accumulated amortization shown as a contra amount for determining the unrecovered balance.

[19] *Notice* at 40769.

[20] *Id.; see also, Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 603 (1944).

[21] *Rate Order*, 8 FCC Rcd at 5795, para. 264.

the range of 10-14% would reflect a reasonable balancing of subscriber and cable operator interests.[22] In the *Notice*, the Commission reached its tentative conclusion of a range of reasonableness from 10-14% based on a summary analysis of the cost of equity and the capital structure of Jate regulated cable services.[23] The *Rate Order* postulated a case-by-case determination of reasonableness regarding the rate of return. As a general approach for evaluation of refund liability from cost of service showings submitted before the effective date of the cost of service rules, we find it appropriate and reasonable to make reference to the range discussed in the *Notice* for our analysis, and to determine the reasonableness of the proffered return in light of that range and of other evidence presented. Chicago Cable's submission included an after-tax overall rate of return of 11.25%. This return is reasonable, and we will accept Chicago Cable's application of an 11.25% rate of return for purposes of our review in this proceeding.

11. **Operating Expenses:** Cable operators may recover in rates their reasonable operating expenses normally associated with providing rate regulated cable services. Our review of Chicago Cable's expenses under general cost of service principles results in adjustments discussed below.

(a) *Depreciation:* At the system level, Chicago Cable includes operating costs of $21,000 under the category "Programming Activities Depreciation Expense." The corresponding asset account, "Programming Production Facilities and Equipment," which represents the asset that is being depreciated, is zero. Chicago Cable provides no explanation of the anomalous situation of depreciating an asset that has zero value. Accordingly, we have disallowed the $21,000 Programming Activities Depreciation Expense.

(b) Similarly, at the corporate level, Chicago Cable includes operating costs of $18,000 under the category "Programming Activities Depreciation Expense." The corresponding asset account is zero. Again, no explanation of this anomalous situation was provided; therefore, we have disallowed the $18,000 Programming Activities Depreciation Expense at the corporate level.

(c) At the system level, Chicago Cable erred in its computation of the entries for the categories "Cable Plant Depreciation Expense," "Plant Support Depreciation Expense," "Selling, General & Administrative Depreciation Expense," and "Amortization Expense-Franchise & Organization Costs." In its filing, Chicago Cable indicates the depreciation or amortization methodology (e.g., ten-year, straight-line) used to determine the referenced depreciation and amortization expenses. However, our review revealed that computation of the entries according to Chicago Cable's specified methodology yields amounts different from those included by Chicago Cable. Consequently, we have recomputed and adjusted the referenced depreciation and amortization expense entries, resulting in the following adjustments:

(i) Cable Plant Depreciation Expense: This item reflects the depreciation expense related to the rate base entries for Headend, Trunk and Distribution Facilities, Drops, and Customer Premises Equipment. (These entries are $5,967,000, $77,056,000, $66,489,000, and $20,153,000, respectively.) Chicago Cable states that it uses a fifteen-year, straight line method of depreciation for headend, trunk and distribution facilities, and drops; and a five-year, straight line method of depreciation for Customer Premises Equipment. Accordingly, the total depreciation should be computed as: [(5,967,000 + 77,056,000 + 66,489,000)/15] + (20,153,000/5) = 13,998,067. Chicago Cable, however, reported $15,076,000 as the Cable Plant Depreciation. The difference of $1,077,933 between our computation and the reported figure is disallowed.

(ii) Plant Support Depreciation Expense: This item reflects the depreciation expense related to the rate base entry for Construction/Maintenance Facilities and Equipment. (This entry is $4,915,000.) Chicago Cable states that it uses a ten-year, straight line method of depreciation for construction, maintenance facilities and equipment. Accordingly, the total depreciation should be computed as: $4,915,000/10=491,500. Chicago Cable, however, reported $757,000 as the Plant Support Depreciation Expense. The difference of $265,500 between our computation and the reported figure is disallowed.

(iii) Selling, General & Administrative Depreciation Expense: This item reflects the depreciation expense related to the entries for "Business Offices Facilities and Equipment" and "Other Tangible Assets." Although Chicago Cable does not provide complete information as to the useful lives of these assets or describe its own methodology for calculating the depreciation expense, rather than disallow the entirety of the depreciation expense, we have calculated an allowable depreciation expense based on the information available. Generally, we recomputed the depreciation expense by estimating the value of the asset, using Chicago Cable's stated 7.5-year life for office equipment and furniture and other tangible assets; and a 40-year life for buildings. Using this estimate, we then determined the depreciation expense for each asset. The difference ($215,733) between the total depreciation expense we calculated and the reported figure is disallowed.

(iv) Amortization Expense-Franchise & Organization Costs: This item reflects the amortization expense related to the entry for "Organizational and Franchise Costs." (This entry is $7,948,000.) Chicago Cable states that it uses a 27-year, straight line method for amortizing its organizational and franchise costs. Accordingly, the total amortization should be com-

[22] *See Notice* at 40765. Since the release of the *Notice*, the Commission has adopted a unitary rate of return for cable of 11.25%. *Cost Order*, 9 FCC Rcd at _____, para. 147. The Commission adopted the 11.25% rate of return on an interim basis, based on evidence in the record. However, the *Cost Order* applies to rate justification filings submitted after the effective date of the rules, and not to filings already pending. *Id.* at 4527, para. 5; *see also, Rate Order*, 8 FCC Rcd at 5854, n.859.

[23] *See Notice* at 40765.

puted as: $7,948,000/27=$294,370. Chicago Cable, however, reported $506,000 as the Amortization Expense-Franchise & Organization Costs. The difference of $211,630 between our computation and the reported figure is disallowed.

IV. CONCLUSION

12. Based on our review of Chicago Cable's cost of service filing and supplemental information, applying general cost of service principles and appropriate allocation rules, we find that, while Chicago Cable's cost of service showing overstates its revenue requirement, Chicago Cable's CPS rate for the period under review, $11.29, is justified based on this showing.[24]

13. Accordingly, IT IS ORDERED, pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321, that the CPS rate charged by Chicago Cable TV with respect to the above-referenced communities, for the period September 1, 1993, to May 14, 1994, of $11.29, IS JUSTIFIED under general cost of service principles and applicable allocation rules, and no refund liability for CPS service during that period will be imposed.[25]

14. IT IS FURTHER ORDERED that the complaints filed against Chicago Cable TV regarding its CPS rate for the period September 1, 1993, to May 14, 1994, ARE DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[24] This finding is based solely on the representations of Chicago Cable in its cost of service filing. Should information come to our attention that these representations (including representations as to the status of *a la carte* packages or data regarding installations and customer equipment) were materially inaccurate, we reserve the right to take appropriate action. This Order is not to be construed as a finding that we have accepted as correct any specific entry, explanation or argument made by any party to this proceeding not specifically addressed herein (including the operator's Form 393).

[25] The findings in this Order do not in any way prejudge the reasonableness of prices for CPS service after May 14, 1994 under our rate regulations. However, to the extent Chicago Cable has sought to take advantage of the refund deferral period under the *Second Order on Reconsideration* (Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, 9 FCC Rcd 4119 (1994)), the CPS rate found reasonable herein might also apply from May 15, 1994 until the date on which Chicago Cable implemented its CPS price under the new regulations.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

U.S. Cable Corporation — CUID Nos. IL1386 (Lake Forest, IL) IL1387 (Lake Bluff, IL)

Cost of Service Filing To Support
Cable Programming Service Rate

MEMORANDUM OPINION AND ORDER

Adopted: November 8, 1994; Released: November 9, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On November 15, 1993, U.S. Cable Corporation ("U.S. Cable") filed a cost of service submission with the Commission in response to complaints that allege that U.S. Cable's cable programming service ("CPS") rate in its Lake Forest and Lake Bluff, Illinois franchises is excessive.[1] On July 7, 1994, U.S. Cable supplemented and amended its filing as permitted by the Bureau's *May 23 Order*.[2]

2. U.S. Cable's cost of service filing seeks to establish that its CPS rate of $17.04 per month for the period September 1,1993, to May 14, 1994, is justified based on U.S. Cable's cost of providing CPS. Our review of the record indicates that, although not all of the costs in U.S. Cable's showing are allowable under general cost of service principles, even if we disallow those non-allowable costs, U.S. Cable's CPS rate in effect for the referenced time period is justified under general cost of service principles.[3]

3. According to information provided by U.S. Cable in its cost of service submission, its system provides service to approximately 4,528 basic subscribers and 4,413 CPS subscribers. U.S. Cable provides 21 channels on its basic tier and 30 channels on its CPS tier. Pursuant to our rules, cable operators are required to present cost of service showings at the franchise level.[4] U.S. Cable has filed its submission for the integrated cable system in Illinois which includes the areas of Lake Forest (CUID No. IL1386) and Lake Bluff (CUID No. IL1387). U.S. Cable maintains that it is appropriate to present its cost of service showings at the system level because U.S. Cable serves both franchise areas through the same cable system, charges the same prices for all cable services and associated equipment in both areas, and offers the same channel line-ups in both areas. U.S. Cable claims that although it is regulated by two separate franchising authorities, it pays the same franchise fees in both areas. Our review of the record indicates that the information provided in U.S. Cable's submission supports these claims. Because there are no significant distinctions between U.S. Cable's services and rates in these two areas, we will permit the single filing.

4. We emphasize that in this review process, pursuant to the 1992 Cable Act, we are analyzing rates for a limited past period, solely for the purpose of determining whether any refund liability has arisen.[5] As discussed below, we are applying general cost of service principles with Commission rules and guidance that were available at the time these filings were made.

II. BACKGROUND

5. On May 3, 1993, the Commission released its *Rate Order* establishing rules to implement the cable television rate regulation provisions of the 1992 Cable Act. In the *Rate Order*, the Commission determined that a benchmark and price cap approach should serve as the primary method for regulating basic service and CPS rates. The Commission also concluded that because the benchmark methodology might not produce fully compensatory rates in all cases, it was appropriate to permit operators, as an alternative, to justify rates based on costs, using individual cost of service showings.[6] The cost of service approach was intended to be used only if an operator believed that the maximum rate permitted under the benchmark formula would not enable the operator to recover costs reasonably incurred in providing rate regulated cable services.

6. The Commission found, however, that the record before it at the time of the adoption of the *Rate Order* did not provide sufficient information on which to develop detailed cost of service rules for the cable industry.[7] Therefore, on July 16, 1993, the Commission issued a Notice of Proposed Rulemaking which proposed requirements to govern cost of service showings submitted by cable oper-

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[1] The earliest of the complaints accepted by the Commission was filed on September 30, 1993.

[2] Cable Operators' Rate Justification Filings, Sections 76.945, 76.956 of the Commission's Rules, Order, DA 94-526 (released May 23, 1994) (*"May 23 Order"*); *see also*, Cable Operators' Rate Justification Filings, Order, DA 94-619 (released June 14, 1994). Prior to the deadline for amending or supplementing cost of service filings, Commission staff contacted U.S. Cable by telephone (with follow-up confirmation letter), to provide the operator with informal guidance as to specific information that staff's preliminary review indicated should be added to or corrected in the operator's pending cost-of-service filing.

[3] This Order does not make any findings or rulings regarding U.S. Cable's rates for basic service and equipment, or premium services. Regulation of rates for basic service and equipment is generally the responsibility of the local franchising authorities, and premium services are unregulated. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) (*"Rate Order"*), at 5637. Data for these services were reviewed only to the extent needed for our evaluation of the reasonableness of an operator's CPS rates.

[4] *See Rate Order*, 8 FCC Rcd at 5977, para. 559; 47 C.F.R. § 76.924(e)(1).

[5] *See* Communications Act of 1934, as amended by the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act"), at § 623(c)(1)(C). The 1992 Cable Act authorizes the Commission to order that the operator refund to subscribers that portion of rates that subscribers have paid after the filing of a valid complaint, that are then found to be unreasonable.

[6] *Rate Order*, 8 FCC Rcd at 5794-95; *see also*, 47 C.F.R. § 76.922.

[7] *Rate Order*, 8 FCC Rcd at 5798-99.

ators seeking to justify rates higher than those determined under the benchmark approach.[8] The Commission indicated in the *Notice,* as it did in the *Rate Order,* that general cost of service principles would apply to cost of service filings submitted prior to the adoption of specific rules.[9] U.S. Cable's cost of service filing under review here was submitted during that pre-adoption time period and covers only the period prior to May 15, 1994. We are analyzing the rates in effect for the period prior to May 15, 1994, as the Commission instructs, under general cost of service principles, not under the rules adopted by the Commission in February 1994.[10]

III. DISCUSSION

7. In analyzing U.S. Cable's cost of service submission, we considered that the cost of service approach permits rates to be set to allow a company to recover the reasonable costs of providing rate regulated cable services, including an opportunity to earn a fair return on its investment."[11] If we find that a certain rate base or expense element is not supported, is excessive, or is unrelated to providing rate regulated cable service, we can disallow that cost in whole or in part.[12] We have evaluated rate base and expense items to determine whether U.S. Cable should be permitted to recover those items in its rates. In some cases, we have found costs that are not allowable, and we have made appropriate adjustments. Even with our adjustments and disallowances, however, we find that U.S. Cable's CPS rate for the period under review has been justified.

8. **Rate Base:** Rate base represents the amount of investment the cable company makes in its facilities to provide service to its customers. Under traditional cost of service principles, it is necessary to determine the allowable rate base in order to calculate the revenue requirement based on the applied rate of return. In analyzing U.S. Cable's filing, we reviewed the components of U.S. Cable's rate base to determine the investment upon which U.S. Cable is entitled to earn a return. For purposes of this review, we made adjustments to the rate base as discussed below.

(a) *Depreciation:* At the time of U.S. Cable's filing, the Commission's rules did not (and do not) specify precise useful lives for several capital asset categories, including headend equipment, trunk and distribution facilities, drops, and customer premises equipment. We have evaluated the reasonableness of depreciable lives assigned to capital asset categories by U.S. Cable and other operators based on cable industry experience as reflected in our surveys and in these and other filings, and, to a lesser degree, experience in the telecommunications industry, where significant capital investments in distribution plant and related equipment are common. [13]

(b) In its filing, U.S. Cable provides gross book values, net book values, accumulated depreciation, and useful lives for each asset. U.S. Cable also provides an allocation key that shows how asset values are allocated at the system level. However, U.S. Cable understates the depreciable lives of its rate base assets, which results in overstatement of the depreciation expense. For example, U.S. Cable reports useful lives of eight years for its head-end, trunk and distribution assets, which represents 81.20% of its tangible gross book value. Operators generally assign fifteen-year useful lives to these assets. In the absence of explanations from U.S. Cable justifying these departures from industry norms, we have made adjustments to the depreciable lives proposed by U.S. Cable to reflect more appropriate useful lives for the categories of capital assets, and have recomputed the net book values and associated depreciation expenses accordingly. These adjustments resulted in disallowances in the provision for depreciation expense includible in the revenue requirement for the development of CPS rates. We have, therefore, adjusted the total investment in property, plant, and equipment included in the rate base to reflect the reduction in accumulated depreciation by the amount of the disallowed depreciation expense. This adjustment results in a $315,590 increase in the CPS portion of net rate base.

(c) *Allocation:* U.S. Cable allocated its net book values to the basic and CPS tiers using a subscriber-weighted channel allocation methodology. The Commission's rules in effect at the time of the U.S. Cable filing specify that costs at the franchise level must be allocated between tiers based on the ratio of channels on each tier to the total number of chan-

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[8] Implementation of Sections of the Cable Television Consumer Protection Act of 1992: Rate Regulation, MM Docket No. 93-215, Notice of Proposed Rulemaking, FCC 93-353 (released July 16, 1993), 58 Fed. Reg. 40762 (July 30, 1993) (*"Notice"*) .

[9] *Id.* at 40703; *Rate Order,* 8 FCC Rcd at 5798-99, 5854, n.859.

[10] In February 1994, the Commission adopted an order setting forth specific regulatory requirements to govern cost of service filings to justify rates above levels determined under its benchmark requirements. The new rules apply to rates charged or to be charged after May 15, 1994. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd 4527 (1994) (*"Cost Order"*).

[11] *See Notice* at 40765:

> Under traditional cost-of-service regulation, rates are set at a level to provide the company with recovery of its costs and a reasonable opportunity to earn a fair return on its invested capital. Under the traditional formulation, the company's revenue requirement is equal to the expenses of providing service and its return on investment.

[12] The Commission made clear that the fact that an operator has incurred costs does not necessarily establish its right to recover those costs from subscribers. *See Rate Order,* 8 FCC Rcd at 5794, n.619. "When electing [to make] a cost of service showing, the cable operator assumes the risk that its rate could be lowered if such action is justified by the cost showing." *Id.* at 5800, para. 272.

[13] We have examined depreciation lives in cable operator cost of service filings to assess cable industry depreciation practices, and we have considered telecommunications industry practices as well. We note that, on average, the depreciation lives reported by cable operators for main cable plant is twelve to fifteen years. In addition, we referred to the Commission's study of depreciation lives for telecommunications plant for use by local exchange carriers. The result of the Commission's study established ranges of 25-30 years for aerial, underground and buried cable. *See* Simplification of the Depreciation Prescription Process, CC Docket No. 92-296, Second Report and Order, FCC 94-174 (released June 28, 1994).

nels offered.[14] We have accordingly reallocated U.S. Cable's net book values to the basic and CPS tiers based on the ratio of channels on each tier to the total number of channels offered.[15] Using the depreciation expense as adjusted above, the reallocation results in a rate base reduction to the CPS tier of $87,722. Overall, these adjustments result in an allowable CPS portion of rate base of $2,707,483.

9. **Rate of Return:** A regulated entity is entitled the opportunity to earn a fair return on investment.[16] That return should be sufficient to ensure confidence in the financial integrity of the enterprise,[17] but should be balanced with our interest in protecting a company's subscribers. In the *Rate Order* the Commission stated that it would make a case-by-case determination of reasonableness for submissions made before specific cost rules could be adopted. [18] In the rulemaking notice initiating a proceeding to adopt such rules, released several weeks before the submission date of these initial cost of service filings, the Commission discussed its analysis of rate of return generally, and tentatively concluded that an after-tax, overall rate of return in the range of 10-14% would reflect a reasonable balancing of subscriber and cable operator interests. [19] In the *Notice,* the Commission reached its tentative conclusion of a range of reasonableness from 10-14% based on a summary analysis of the cost of equity and the capital structure of regulated cable services.[20] The *Rate Order* postulated a case-by-case determination of reasonableness regarding the rate of return. As a general approach for evaluation of refund liability from cost of service showings submitted before the effective date of the cost of service rules, we find it appropriate and reasonable to make reference to the range discussed in the *Notice* for our analysis, and to determine the reasonableness of the proffered return in light of that range and of other evidence presented. U.S. Cable's submission includes an after-tax overall rate of return of 11.25%. This return is reasonable, and we will accept U.S. Cable's application of an 11.25% rate of return for purposes of our review in this proceeding.

10. **Operating Expenses:** Cable operators may recover in rates their reasonable expenses normally associated with providing rate regulated cable services. Our review of U.S. Cable's expenses under general cost of service principles, results in the following adjustments. As discussed with respect to the rate base, we have adjusted U.S. Cable's depreciation expenses to reflect longer expected useful lives than reflected in U.S. Cable's cost of service filing. Similarly, we have adjusted U.S. Cable's aggregate CPS depreciation expense to reflect longer useful lives. These adjustments produce a disallowance of $99,513 to U.S. Cable's depreciation expense.[21]

IV. CONCLUSION

11. Based on our review of U.S. Cable's cost of service filing and supplemental information, applying general cost of service principles and applicable cost allocation rules, we find that, while U.S. Cable's cost of service showing overstates its revenuerequirement, the CPS rate U.S. Cable seeks to justify for the period under review, $17.04, is supported by this showing.[22]

12. Accordingly, IT IS ORDERED, pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321, that the CPS rate charged by U.S. Cable Corporation with respect to the above-referenced communities, for the period September 1, 1993, to May 14, 1994, of $17.04, IS JUSTIFIED under general cost of service principles and applicable allocation rules, and that no refund liability for CPS service during that period will be imposed.[23]

13. IT IS FURTHER ORDERED that the complaints filed against U.S. Cable Corporation regarding its CPS rate for the period September 1, 1993, to May 14, 1994, ARE DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

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[14] *See Rate Order,* 8 FCC Rcd at 5976

[15] 47 C.F.R. § 76.924(e)(2).

[16] *Notice* at 40769.

[17] *Id.; see also, Federal Power Commission v. Hope Natural Gas Company,* 320 U.S. 591, 603 (1944).

[18] *Rate Order,* 8 FCC Rcd at 5795, para. 264.

[19] *See Notice* at 40765. Since the release of the *Notice,* the Commission has adopted a unitary rate of return for cable of 11.25%. *Cost Order,* 9 FCC Rcd at _____, para. 147. The Commission adopted the 11.25% rate of return on an interim basis, based on evidence in the record. However, the *Cost Order* applies to rate justification filings submitted after the effective date of the rules, and not to filings already pending. *Id.* at 4527, para. 5; *see also, Rate Order,* 8 FCC Rcd at 5854, n.859.

[20] *See Notice* at 40765. A

[21] This adjustment reflects the use of longer lives as well as the reallocation of expenses using the per channel allocation methodology required by the Commission rules.

[22] This finding is based solely on the representations of U.S. Cable in its cost of service filing. Should information come to our attention that these representations (including representations as to the status of *a la carte* packages or data regarding installations and customer equipment) were materially inaccurate, we reserve the right to take appropriate action. This Order is not to be construed as a finding that we have accepted as correct any specific entry, explanation or argument made by any party to this proceeding not specifically addressed herein (including the operator's Form 393).

[23] The findings in this Order do not in any way prejudge the reasonableness of prices for CPS service after May 14, 1994 under our rate regulations. However, to the extent U.S. Cable has sought to take advantage of the refund deferral period under the *Second Order on Reconsideration* (Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, 9 FCC Rcd 4119 (1994)), the CPS rate found reasonable herein might also apply from May 15, 1994 until the date on which U.S. Cable implemented its CPS price under the new regulations.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

United Video Cablevision, Inc.	CUID Nos. MA0333 (Berlin, MA) MA0334 (Harvard, MA)

Cost of Service Filing To Support
Cable Programming Service Rate

MEMORANDUM OPINION AND ORDER

Adopted: November 8, 1994; Released: November 9, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On February 25, 1994, United Video Cablevision, Inc. ("United Video") filed a cost of service submission with the Commission in response to complaints that allege that United Video's cable programming service ("CPS") rate in its Harvard and Berlin, Massachusetts franchises is excessive.[1] On July 14, 1994, United Video supplemented and amended its filing as permitted by the Bureau's *May 23 Order*. [2]

2. United Video's cost of service filing seeks to establish that its CPS rate of $11.35 per month for the period September 1, 1993, to May 14, 1994, is justified based on United Video's cost of providing CPS. Our review of the record indicates that, although not all of the costs in United Video's showing are allowable under general cost of service principles, even if we disallow those non-allowable costs, United Video's CPS rate in effect for the referenced time period is justified under general cost of service principles, as discussed below.[3]

3. According to information provided by United Video in its cost of service submission, United Video's Berlin/Harvard system provides service to approximately 1,614 basic subscribers and 1,496 CPS subscribers. United Video provides 24 channels on its basic tier and 23 channels on its CPS tier. Pursuant to our rules, cable operators are required to present cost of service showings at the franchise level.[4] United Video has filed its submission for a cable system comprised of the towns of Berlin (MA0333) and Harvard (MA0334) in Massachusetts. United Video states that all subscribers to the system receive the same services, at the same rates, using the same physical facilities. Our review of the record indicates that the information provided in United Video's submission supports these claims. Because there are no significant distinctions between United Video's services and rates in these two areas, we will permit the single filing.

4. We emphasize that in this review process, pursuant to the 1992 Cable Act, we are analyzing rates for a limited past period, solely for the purpose of determining whether any refund liability has arisen.[5] As discussed below, we are applying general cost of service principles with Commission rules and guidance that were available at the time these filings were made.

II. BACKGROUND

5. On May 3, 1993, the Commission released its *Rate Order* establishing rules to implement the cable television rate regulation provisions of the 1992 Cable Act. In the *Rate Order*, the Commission determined that a benchmark and price cap approach should serve as the primary method for regulating basic service and CPS rates. The Commission also concluded that because the benchmark methodology might not produce fully compensatory rates in all cases, it was appropriate to permit operators, as an alternative, to justify rates based on costs, using individual cost of service showings.[6] The cost of service approach was intended to be used only if an operator believed that the maximum rate permitted under the benchmark formula would not enable the operator to recover costs reasonably incurred in providing rate regulated cable services.

6. The Commission found, however, that the record before it at the time of the adoption of the *Rate Order* did not provide sufficient information on which to develop

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[1] The earliest of the complaints accepted by the Commission was filed on February 2, 1994. United Video argues in a cover letter to its cost of service filing that FCC Form 329 is defective because it fails to require anything "that could reasonably be characterized a description' as required by [our rules]." FCC Form 329 requires that complainants describe and characterize the services complained of, and attach a current bill for services. We find that this Form provides sufficient information to allow us to adjudicate these complaints, and we reject United Video's informal request that complaints be dismissed on this basis.

[2] Cable Operators' Rate Justification Filings, Sections 76.945, 76.956 of the Commission's Rules, Order, DA 94-526 (released May 23, 1994) (*"May 23 Order"); see also,* Cable Operators' Rate Justification Filings, Order, DA 94-619 (released June 14, 1994). Prior to the deadline for amending or supplementing cost of service filings, Commission staff contacted United Video by telephone (with follow-up confirmation letter), to provide the operator with informal guidance as to specific information that staff's preliminary review indicated should be added to or corrected in the operator's pending cost-of-service filing.

[3] This Order does not make any findings or rulings regarding United Video's rates for basic service and equipment, or premium services. Regulation of rates for basic service and equipment is generally the responsibility of the local franchising authorities, and premium services are unregulated. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) (*"Rate Order"*), at 5637. Data for these services were reviewed only to the extent needed for our evaluation of the reasonableness of an operator's CPS rates.

[4] *See Rate Order,* 8 FCC Rcd at 5977, para. 559; 47 C.F.R. § 76.924(e)(1).

[5] *See* Communications Act of 1934, as amended by the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act"), at § 623(c)(1)(C). The 1992 Cable Act authorizes the Commission to order that the operator refund to subscribers that portion of rates paid after the filing of a valid complaint, that are then found to be unreasonable.

[6] Rate Order , 8 FCC Rcd at 5794-95; *see also,* 47 C.F.R. § 76.922.

detailed cost of service rules for the cable industry.[7] Therefore, on July 16, 1993, the Commission issued a Notice of Proposed Rulemaking which proposed requirements to govern cost of service showings submitted by cable operators seeking to justify rates higher than those determined under the benchmark approach.[8] The Commission indicated in the *Notice*, as it did in the *Rate Order*, that general cost of service principles would apply to cost of service filings submitted prior to the adoption of specific rules.[9] United Video's cost of service filing under review here was submitted during that pre-adoption time period and covers only the period prior to May 15, 1994. We are analyzing the rates in effect for the period prior to May 15, 1994, as the Commission instructs, under general cost of service principles, not under the rules adopted by the Commission in February 1994.[10]

III. DISCUSSION

7. In analyzing United Video's cost of service submission, we considered that the cost of service approach permits rates to be set to allow a company to recover the reasonable costs of providing rate regulated cable services, including an opportunity to earn a fair return on its investment.[11] If we find that a certain rate base or expense element is not supported, is excessive, or is unrelated to providing rate regulated cable service, we can disallow that cost in whole or in part.[12] We have evaluated rate base and expense items to determine whether United Video should be permitted to recover those items in its rates. In some cases, we have found costs that are not allowable, and we have made appropriate adjustments. Even with our adjustments and disallowances, however, we find that United Video's CPS rate for the period under review has been justified.

8. **Rate Base:** Rate base represents the amount of investment the cable company makes in its facilities to provide service to its customers. Under traditional cost of service principles, it is necessary to determine the allowable rate base in order to calculate the revenue requirement based on the applied rate of return. For the CPS service category, United Video claimed a rate base value of $333,556. In analyzing United Video's filing, we reviewed the components of United Video's rate base to determine the investment for providing CPS service upon which United Video is entitled to earn a return. We find it necessary to make allocation adjustments as discussed below.

(a) *Allocation:* United Video records costs at the state level, and uses various allocators to distribute costs from the Massachusetts state level to the Berlin/Harvard system level.[13] This results in both overstated and understated allocations. The Commission's rules in effect at the time of the United Video filing specify that operators are to allocate expenses and revenues aggregated at higher levels to the franchise level based on the ratio of the total number of subscribers served at the franchise level to the total number of subscribers served at the higher level.[14] Instead of United Video's various allocation methodologies, the rules stipulate a single allocation based on the number of subscribers. We have accordingly reallocated United Video's state level net book values to the system level using the appropriate allocation factor, which for the Berlin/Harvard system is a subscriber ratio of 6.54%. We then allocated the system level net book values to the basic and CPS tiers based on the ratio of channels on each tier to the total number of channels offered.[15] This results in a rate base reduction of $120,694.

9. **Rate of Return:** A regulated entity is entitled to the opportunity to earn a fair return on investment.[16] That return should be sufficient to ensure confidence in the financial integrity of the enterprise, [17] but should be balanced with our interest in protecting a company's subscribers. In the *Rate Order* the Commission stated that it would make a case-by-case determination of reasonableness for submissions made before specific cost rules could be adopted.[18] In the rulemaking notice initiating a proceeding to

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[7] *Rate Order*, 8 FCC Rcd at 5798-99.

[8] Implementation of Sections of the Cable Television Consumer Protection Act of 1992: Rate Regulation, MM Docket No. 93-215, Notice of Proposed Rulemaking, FCC 93-353 (released July 16, 1993), 58 Fed. Reg. 40762 (July 30, 1993) (*"Notice"*).

[9] *Id.* at 40763; *Rate Order*, 8 FCC Rcd at 5798-99, 5854, n.859.

[10] In February 1994, the Commission adopted an order setting forth specific regulatory requirements to govern cost of service filings to justify rates above levels determined under its benchmark requirements. The new rules apply to rates charged or to be charged after May 15, 1994. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd 4527 (1994) (*"Cost Order"*).

[11] *See Notice* at 40755:

> Under traditional cost-of-service regulation, rates are set at a level to provide the company with recovery of its costs and a reasonable opportunity to earn a fair return on its invested capital. Under the traditional formulation, the company's revenue requirement is equal to the expenses of providing service and its return on investment.

[12] The Commission made clear that the fact that an operator has incurred costs does not necessarily establish its right to recover those costs from subscribers. *See Rate Order*, 8 FCC Rcd at 5794, n.619. "When electing [to make] a cost of service showing, the cable operator assumes the risk that its rate could be lowered if such action is justified by the cost showing." *Id.* at 5800, para. 272.

[13] United Video shows calculations at two levels, "state" meaning all its operations within Massachusetts, and "system" meaning its operations in the Berlin and Harvard communities.

[14] *See Rate Order*, 8 FCC Rcd at 5976. Under the Commission rules in effect at the time of this filing, operators are required to aggregate expenses and revenues at either the franchise, system, regional, or company level in a manner consistent with the practices of the operator as of April 3, 1993. 47 C.F.R. § 76.924(d). Costs aggregated at a higher level are to be allocated to the franchise level in proportion to the number of subscribers in the franchise area. 47 C.F.R. § 76.924(e)(1).

[15] *Id.* Costs allocated to the franchise level must be allocated between tiers in proportion to the number of channels on each tier. 47 C.F.R. §§ 76.924(e)(2). This requirement does not apply to programming costs, franchise fees, or public, education and government access costs, which are allocated entirely to the basic tier or directly assigned as appropriate.

[16] *Notice* at 40769.

[17] *Id.; see also, Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 603 (1944).

[18] *Rate Order*, 8 FCC Rcd at 5795, para. 264.

adopt such rules, released several weeks before the submission date of these initial cost of service filings, the Commission discussed its analysis of rate of return generally, and tentatively concluded that an after-tax, overall rate of return in the range of 10-14% would reflect a reasonable balancing of subscriber and cable operator interests.[19]

(a) In the *Notice*, the Commission reached its tentative conclusion of a range of reasonableness from 10-14% based on a summary analysis of the cost of equity and the capital structure of regulated cable services.[20] The *Rate Order* postulated a case-by-case determination of reasonableness regarding the rate of return. As a general approach for evaluation of refund liability from cost of service showings submitted before the effective date of the cost of service rules, we find it appropriate and reasonable to make reference to the range discussed in the *Notice* for our analysis, and to determine the reasonableness of the proffered return in light of that range and of other evidence presented. In the absence of argument by United Video that justifies a higher rate of return, for purposes of examining United Video's filing in this case, we will use an after-tax, overall rate of return within that range.

(b) United Video's submission includes a pre-tax overall rate of return of 18.9%[21] As an alternative, United Video suggests use of the Commission's 11.25% after-tax rate of return[22] as established in the *Cost Order*. [23] The Commission's cost of service analysis is traditionally based on an after-tax rate of return. We find United Video's use of an 11.25% after-tax rate of return reasonable, and have reviewed its showing in that light. We find that United Video overstates its return on investment by $96,502, using an 11.25% rate of return, and we have made adjustments to its revenue requirement accordingly. However, even with this disallowance, United Video has justified its rate for the period under review.

10. **Operating Expenses:** Cable operators may recover in rates their reasonable expenses normally associated with providing rate regulated cable services. United Video claims total operating expenses of $258,860. We have evaluated several of United Video's expense items and believe that, in addition to incorrect allocations, certain items are questionable. However, even if the amounts associated with these items are disallowed and allocated in accordance with the rules, United Video has justified its CPS rate for the period in question.

(a) *Allocation:* As previously stated, United Video fails to allocate from the state level to the franchise level on the basis of subscribers as required under the Commission's rules. We computed the allocator to be applied and adjusted operating expense amounts allocated to the franchise level to reflect the methodology required under our rules.

(b) *Depreciation:* In its filing, United Video identifies 30 line items as rate base assets. United Video provides gross book values, net book values, accumulated depreciation, and useful lives for each such asset. The Commission's rules did not (and do not) specify precise useful lives for several capital asset categories, including headend equipment, trunk and distribution facilities, drops, and customer premises equipment. We have evaluated the reasonableness of depreciable lives assigned to capital asset categories by United Video and other operators based on cable industry experience as reflected in our surveys and in these and other filings, and, to a lesser degree, experience in the telecommunications industry, where significant capital investments in distribution plant and related equipment are common.[24] United Video has not provided any explanation to justify the eight-year depreciation lives it uses for headend, trunk and distribution equipment, although these vary substantially from what we believe to be industry norms. For purposes of this examination, we have made adjust-

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[19] *See Notice* at 40765. Since the release of the *Notice*, the Commission has adopted a unitary rate of return for cable of 11.25%. *Cost Order*, 9 FCC Rcd at _____, para. 147. The Commission adopted the 11.25% rate of return on an interim basis, based on evidence in the record. However, the *Cost Order* applies to rate justification filings submitted after the effective date of the rules, and not to filings already pending. *Id.* at 4527, para. 5; *see also, Rate Order*, 8 FCC Rcd at 5854, n.859.

[20] *See Notice* at 40765.

[21] United Video based its analysis on "materials in the record of the ongoing rulemaking proceeding regarding cost-of-service showings. Specifically, United Video used evidence from the cost-of-service rulemaking record to estimate a reasonable pre-tax overall return on rate base." United Video, February 25, 1994, Cost of Service Rate Justification Submission at page 7 (emphasis added). The Commission, however, has traditionally calculated rate of return after taxes, and has continued to do so in the case of cable rate regulation.

[22] United claims that use of the after-tax 11.25% produces a pre-tax return of 20.27%. However, United Video has incorrectly calculated the return amount subject to income taxes, and its pre-tax rate of 20.27% is not accurate. In our review of United Video's submission, we find that United Video's interest charges exceed its return on rate base, meaning that its non-taxable interest charge is larger than its taxable return. (Although it is not specifically reported by United Video, we have estimated the applicable system level share of interest charges to be $572,904. The allocable shares to basic service and CPS, based on assignments by channel ratios, are $241,250 and $231,167, respectively. These amounts greatly exceed the basic service and CPS shares of return on rate base.) Thus, no tax liability is incurred, and no allowance, or gross-up, for income tax results.

[23] United Video, February 25, 1994 Cost of Service Rate Justification Submission, at n.17.

[24] We have examined depreciation lives in cable operator cost of service filings to assess cable industry depreciation practices, and we have considered telecommunications industry practices as well. We note that, on average, the depreciation lives reported by cable operators for main cable plant is twelve to fifteen years. In addition, we referred to the Commission's study of depreciation lives for telecommunications plant for use by local exchange carriers. The result of the Commission's study established ranges of 25-30 years for aerial, underground and buried cable. *See* Simplification of the Depreciation Prescription Process, CC Docket No. 92-296, Second Report and Order, FCC 94-174 (released June 28, 1994).

ments to reflect more usual depreciation lives[25] for buildings and headend, trunk and distribution facilities.[26]

(c) The cumulative effect of disallowance of expenses described in (a) and (b) above is a reduction of $67,274 in United Video's revenue requirement. However, even with these adjustments to United Video's operating expenses, the CPS rate charged by United Video is justified.

11. **Revenue Offsets:** In its supplemental filing, United Video identifies Home Shopping, Marketing, and Other Revenues received, but does not include these revenues as adjustments to its total revenue requirement computations. In our calculations, we have reduced United Video's revenue requirement by the dollar amounts associated with these revenues, producing a reduction to United Video's revenue requirement of $4,935. Even with this disallowance, United Video's CPS rate is justified and does not create a refund obligation for the period under review.

IV. CONCLUSION

12. Based on our review of United Video's cost of service filing and supplemental information, applying general cost of service principles and applicable cost allocation rules, we find that, while United Video's cost of service showing overstates its revenue requirement, the CPS rate United Video seeks to justify for the period under review, $11.35, is supported by this showing.[27]

13. Accordingly, IT IS ORDERED, pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321, that the CPS rate of $11.35 charged by United Video Cablevision, Inc. with respect to the above-referenced communities, for the period September 1, 1993, to May 14, 1994, IS JUSTIFIED under general cost of service principles and applicable cost allocation rules, and that no refund liability for CPS service during that period will be imposed.[28]

14. IT IS FURTHER ORDERED that the complaints filed against United Video Cablevision, Inc. regarding its CPS rate for the period September 1, 1993, to May 14, 1994, ARE DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

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[25] We have also recomputed rate base assets for the period under review to reflect adjustments to depreciable lives. This adjustment does not result in any refund liability.

[26] United Video assigns a useful life of ten years to its buildings. We believe that buildings can be expected to be used over a substantially longer period than ten years, and we have used a forty-year life, common in regulatory accounting, for this examination, and have made adjustments to depreciation expense accordingly. Similarly, United Video assigns headend, trunk and distribution equipment a useful life of eight years. We believe the industry norm is closer to twelve to fifteen years, and we have made adjustments to reflect fifteen year lives for headend, trunk and distribution equipment for purposes of this review. None of these adjustments results in any refund liability in this case.

[27] This finding is based solely on the representations of United Video in its cost of service filing. Should information come to our attention that these representations (including representations as to the status of *a la carte* packages or data regarding installations and customer equipment) were materially inaccurate, we reserve the right to take appropriate action. This Order is not to be construed as a finding that we have accepted as correct any specific entry, explanation or argument made by any party to this proceeding not specifically addressed herein (including the operator's Form 393).

[28] The findings in this Order do not in any way prejudge the reasonableness of prices for CPS service after May 14, 1994 under our rate regulations. However, to the extent United Video has sought to take advantage of the refund deferral period under the *Second Order on Reconsideration* (Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, 9 FCC Rcd 4119 (1994)), the CPS rate found reasonable herein might also apply from May 15, 1994 until the date on which United Video implemented its CPS price under the new regulations.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

District Cablevision, L.P. CUID No. DC0002 (Washington, DC)

Cost of Service Filing To Support
Cable Programming Service Rate

MEMORANDUM OPINION AND ORDER

Adopted: November 8, 1994; Released: November 9, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On March 22,1994, District Cablevision, L.P. ("District Cablevision") filed a cost of service submission with the Commission in response to complaints[1] that allege that District Cablevision's cable programming service ("CPS") rate in its Washington, D.C. franchise is excessive.[2] On July 14, 1994, District Cablevision supplemented and amended its filing as permitted by the Bureau's *May 23 Order*.[3]

2. District Cablevision's cost of service filing seeks to establish that its CPS rate of $12.66 per month for the period September 1, 1993, to May 14, 1994, is justified based on District Cablevision's cost of providing CPS. Our review of the record indicates that, although not all of the costs in District Cablevision's showing are allowable under general cost of service principles, even if we disallow those non-allowable costs, District Cablevision's CPS rate in effect for the referenced time period is justified under general cost of service principles[4]

3. According to information provided by District Cablevision in its cost of service submission, District Cablevision's system provides service to approximately 84,072 basic subscribers and 82,284 CPS subscribers. District Cablevision provides 23 channels on its basic tier and 29 channels on its CPS tier.

4. We emphasize that in this review process, pursuant to the 1992 Cable Act, we are analyzing rates for a limited past period, solely for the purpose of determining whether any refund liability has arisen.[5] As discussed below, we are applyingh general cost of service principles with Commission rules and guidance that were available at the time these filings were made.

II. BACKGROUND

5. On May 3, 1993, the Commission released its *Rate Order* establishing rules to implement the cable television rate regulation provisions of the 1992 Cable Act. In the *Rate Order*, the Commission determined that a benchmark and price cap approach should serve as the primary method for regulating basic service and CPS rates. The Commission also concluded that because the benchmark methodology might not produce fully compensatory rates in all cases, it was appropriate to permit operators, as an alternative, to justify rates based on costs, using individual cost of service showings.[6] The cost of service approach was intended to be used only if an operator believed that the maximum rate permitted under the benchmark formula would not enable the operator to recover costs reasonably incurred in providing rate regulated cable services.

6. The Commission found, however, that the record before it at the time of the adoption of the *Rate Order* did not provide sufficient information on which to develop detailed cost of service rules for the cable industry.[7] Therefore, on July 16, 1993, the Commission issued a Notice of Proposed Rulemaking which proposed requirements to govern cost of service showings submitted by cable operators seeking to justify rates higher than those determined

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[1] The earliest of the complaints accepted by the Commission was filed on November 16, 1993.

[2] District Cablevision seeks confidential treatment of Appendices B and C to Exhibit 2, of its March 22, 1994, cost of service submission. For purposes of this proceeding, our review and determination of District Cablevision's CPS cost of service rate was based on non-confidential information provided by District Cablevision in its initial submission and its subsequent July 14, 1994, submission. The July 14, 1994, submission was provided on FCC Form 1220 (the cost of service form required for establishing cost-based rates for post-May 15, 1994 period). Given that our findings of District Cablevision's rate justification are not based on the materials for which District Cablevision seeks confidential treatment, we need not address District Cablevision's request for confidential treatment of those materials at this time.

[3] Cable Operators' Rate Justification Filings, Sections 76.945, 76.956 of the Commission's Rules, Order, DA 94-526 (released May 23, 1994) (*"May 23 Order"*); *see also,* Cable Operators' Rate Justification Filings, Order, DA 94-619 (released June 14, 1994). Prior to the deadline for amending or supplementing cost of service filings, Commission staff contacted District Cablevision by telephone (with follow-up confirmation letter), to provide the operator with informal guidance as to specific information that staff's preliminary review indicated should be added to or corrected in the operator's pending cost-of-service filing.

[4] This Order does not make any findings or rulings regarding District Cablevision's rates for basic service and equipment, or premium services. Regulation of rates for basic service and equipment are generally the responsibility of the local franchising authorities, and premium services are unregulated. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) (*"Rate Order"*), at 5637. Data for these services were reviewed only to the extent needed for our evaluation of the reasonableness of an operator's CPS rates.

[5] *See* Communications Act of 1934, as amended by the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act"), at § 623(c)(1)(C). The 1992 Cable Act authorizes the Commission to order that the operator refund to subscribers that portion of rates that subscribers have paid after the filing of a valid complaint, that are then found to be unreasonable.

[6] *Rate Order,* 8 FCC Rcd at 5794-95; *see also,* 47 C.F.R. § 76.922.

[7] *Rate Order,* 8 FCC Rcd at 5798-99.

under the benchmark approach.[8] The Commission indicated in the *Notice*, as it did in the *Rate Order*, that general cost of service principles would apply to cost of service filings submitted prior to the adoption of specific rules.[9] District Cablevision's cost of service filing under review here was submitted during that pre-adoption time period and covers only the period prior to May 15, 1994. We are analyzing the rates in effect for the period prior to May 15, 1994, as the Commission instructs, under general cost of service principles, not under the rules adopted by the Commission in February 1994.[10]

III. DISCUSSION

7. In analyzing District Cablevision's cost of service submission, we considered that the cost of service approach permits rates to be set to allow a company to recover the reasonable costs of providing rate regulated cable services, including an opportunity to earn a fair return on its investment.[11] If we find that a certain rate base or expense element is not supported, is excessive, or is unrelated to providing rate regulated cable service, we can disallow that cost in whole or in part.[12] We have evaluated rate base and expense items to determine whether District Cablevision should be permitted to recover those items in its rates. In some cases, we have found costs that are not allowable, and we have made appropriate adjustments. Even with our adjustments and disallowances, however, we find that District Cablevision's CPS rate for the period under review has been justified.

8. **Rate Base:** Rate base represents the amount of investment the cable company makes in its facilities to provide service to its customers. Under traditional cost of service principles, it is necessary to determine the allowable rate base in order to calculate the revenue requirement based on the applied rate of return. In analyzing District Cablevision's filing, we reviewed the components of District Cablevision's rate base to determine the investment upon which District Cablevision is entitled to earn a return. For purposes of this review, we made adjustments to the rate base as discussed below.

(a) District Cablevision claims property, plant and equipment $157,000 in excess of those amounts reported on its balance sheet for December 31, 1993, the end of the test year for the data filed. The discrepancy between the amounts stated in District Cablevision's financial statements and the cost of service submission was unexplained. Based on the information before us, we have relied on District Cablevision's audited financial statements, and have disallowed the excess amount from rate base.

(b) District Cablevision includes an amount for Plant Under Construction of $19,000. Under general cost of service principles, allowable costs in rate base are associated with plant that is used and useful. Since there is no indication that this plant was used and useful at the time of filing, for purposes of our analysis we have removed the amount reported as plant under construction from the rate base and made appropriate adjustments to the CPS revenue requirement.

9. **Rate of Return:** A regulated entity is entitled the popportunity to earn a return on investment.[13] That return should be sufficient to ensure confidence in the financial integrity of the enterprise,[14] but should be balanced with our interest in protecting a company's subscribers. In the *Rate Order* the Commission stated that it would make a case-by-case determination of reasonableness for submissions made before specific cost rules could be adopted.[15] In the rulemaking notice initiating a proceeding to adopt such rules, released several weeks before the submission date of these initial cost of service filings, the Commission discussed its analysis of rate of return generally, and tentatively concluded that an after-tax, overall rate of return in the range of 10-14% would reflect a reasonable balancing of subscriber and cable operator interests.[16] In the *Notice*, the Commission reached its tentative conclusion of a range of reasonableness from 10-14% based on a summary analysis of the cost of equity and the capital structure of regulated cable services.[17] The *Rate Order* postulated a case-by-case determination of reasonableness regarding the rate of return. As a general approach for evaluation of refund liability from cost of service showings submitted

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[8] Implementation of Sections of the Cable Television Consumer Protection Act of 1992: Rate Regulation, MM Docket No. 93-215, Notice of Proposed Rulemaking, FCC 93-353, released July 16, 1993, 58 Fed. Reg. 40762 (July 30, 1993) (*"Notice"*) .

[9] *Id.* at 40763; *Rate Order*, 8 FCC Rcd at 5798-99, 5854, n.859.

[10] In February 1994, the Commission adopted an order setting forth specific regulatory requirements to govern cost of service filings to justify rates above levels determined under its benchmark requirements. The new rules apply to rates charged or to be charged after May 15, 1994. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd 4527 (1994) (*"Cost Order"*).

[11] *See Notice* at 40765:

> Under traditional cost-of-service regulation, rates are set at a level to provide the company with recovery of its costs and a reasonable opportunity to earn a fair return on its invested capital. Under the traditional formulation, the company's revenue requirement is equal to the expenses of providing service and its return on investment.

[12] The Commission made clear that the fact that an operator has incurred costs does not necessarily establish its right to recover those costs from subscribers. *See Rate Order*, 8 FCC Rcd at 5794, n.619. "When electing [to make] a cost of service showing, the cable operator assumes the risk that its rate could be lowered if such action is justified by the cost showing." *Id.* at 5800, para. 272.

[13] *Notice* at 40769.

[14] *Id.; see also, Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 603 (1944).

[15] *Rate Order*, 8 FCC Rcd at 5795, para. 264.

[16] *See Notice* at 40765. Since the release of the *Notice*, the Commission has adopted a unitary rate of return for cable of 11.25%. *Cost Order*, 9 FCC Rcd at _____, para. 147. The Commission adopted the 11.25% rate of return on an interim basis, based on evidence in the record. However, the *Cost Order* applies to rate justification filings submitted after the effective date of the rules, and not to filings already pending. *Id.* at 4527, para. 5; *see also, Rate Order*, 8 FCC Rcd at 5854, n.859.

[17] *See Notice* at 40765.

before the effective date of the cost of service rules, we find it appropriate and reasonable to make reference to the range discussed in the *Notice* for our analysis, and to determine the reasonableness of the proffered return in light of that range and of other evidence presented. District Cablevision's submission included an after-tax overall rate of return of 11.25%. This return is reasonable, and we will accept District Cablevision's application of an 11.25% rate of return for purposes of our review in this proceeding.

10. **Operating Expenses:** Cable operators may recover in rates their reasonable operating expenses normally associated with providing rate regulated cable services. Our review of District Cablevision's expenses under general cost of service principles results in the adjustments discussed below.

(a) We find the amount of Cable Plant Depreciation Expense to be approximately $706,940 in excess of depreciation amounts calculated, on a straight-line basis, from the asset values and useful lives information provided in District Cablevision's filing. We have disallowed the excess amount.

(b) District Cablevision includes Programming Activities Depreciation Expenses of $23,000, but the corresponding asset is valued at zero. District Cablevision provides no explanation of a depreciation expense attached to a zero-value asset, and we have, therefore, disallowed the amount of $23,000.

(c) In its operating expenses, District Cablevision includes Franchise Costs Amortization Expenses calculated on an amortization period of fifteen years. However, District Cablevision indicates in its filing that these expenses were amortized over a period of 40 years. We have excluded $178,700 from District Cablevision's operating expenses to reflect the longer amortization period.

IV. CONCLUSION

11. Based on our review of District Cablevision's cost of service filing and supplemental information, applying general cost of service principles, we find that, while District Cablevision's cost of service showing overstates its revenue requirement, its CPS rate for the period under review, $12.66, is justified.[18]

12. Accordingly, IT IS ORDERED, pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321, that the CPS rate charged by District Cablevision, L.P. with respect to the above-referenced community, for the period September 1, 1993, to May 14, 1994, of $12.66, IS JUSTIFIED, and no refund liability for CPS rates during that period will be imposed.[19]

13. IT IS FURTHER ORDERED that the complaints filed against District Cablevision, L.P. regarding its CPS rate for the period September 1, 1993, to May 14, 1994, ARE DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[18] This finding is based solely on the representations of District Cablevision in its cost of service filing. Should information come to our attention that these representations (including representations as to the status of *a la carte* packages or data regarding installations and customer equipment) were materially inaccurate, we reserve the right to take appropriate action. This Order is not to be construed as a finding that we have accepted as correct any specific entry, explanation or argument made by any party to this proceeding not specifically addressed herein (including the operator's Form 393).

[19] The findings in this Order do not in any way prejudge the reasonableness of prices for CPS service after May 14, 1994 under our rate regulations. However, to the extent District Cablevision has sought to take advantage of the refund deferral period under the *Second Order on Reconsideration* (Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, 9 FCC Rcd 4119 (1994)), the CPS rate found reasonable herein might also apply from May 15, 1994 until the date on which District Cablevision implemented its CPS price under the new regulations.

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-56

In the Matter of

Amendment of Section 73.202(b), RM-8459
Table of Allotments,
FM Broadcast Stations.
(Borger, Texas)

REPORT AND ORDER
(Proceeding Terminated)

Adopted: November 21, 1994; Released: November 29, 1994

By the Acting Chief, Allocations Branch:

1. At the request of Zia Broadcasting Company ("petitioner"), licensee of Station KQTY(AM), Borger, Texas, the Commission has before it the *Notice of Proposed Rule Making*, 9 FCC Rcd 3358 (1994), proposing the allotment of Channel 294A to Borger, Texas, as the community's second local FM service. Petitioner filed comments reiterating its intention to apply for Channel 294A, if allotted to Borger.[1] No other comments were received.

2. We believe the public interest would be served by the allotment of Channel 294A to Borger, since it would provide the community with an additional local aural transmission service. Channel 294A can be allotted to Borger in compliance with the Commission's minimum distance separation requirements without the imposition of! a site restriction.[2]

3. Accordingly, pursuant to the authority contained in Sections 4(i), 5(c)(1), 303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61, 0.204(b) and 0.283 of the Commission's Rules, IT IS ORDERED, That effective **January 13, 1995**, the FM Table of Allotments, Section 73.202(b) of the Commission's Rules, IS AMENDED, with respect to the community listed below, to read as follows:

City	Channel No.
Borger, Texas	282C1, 294A

4. The window period for filing applications will open on **January 13, 1995**, and close on **February 13, 1995**.

5. IT IS FURTHER ORDERED, That this proceeding IS TERMINATED.

6. For further information concerning this proceeding, contact Pam Blumenthal, Mass Media Bureau, (202) 634-6530.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

[1] As stated in the *Notice*, petitioner's request, although signed, failed to include an affidavit verifying statements contained in its petition, as required by Section 1.52 of the Commission's Rules. Petitioner was requested to correct the deficiency in its responsive comments, and has complied accordingly by filing a statement.

[2] The coordinates for Channel 294A at Borger are North Latitude 35-39-24 and West Longitude 101-23-36.

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-138

In the Matter of

Amendment of Section 73.202(b), RM-8542
Table of Allotments,
FM Broadcast Stations.
(Ketchikan, Alaska)

NOTICE OF PROPOSED RULE MAKING

Adopted: November 18, 1994; Released: November 29, 1994

Comment Date: January 19, 1995
Reply Comment Date: February 3, 1995

By the Acting Chief, Allocations Branch:

1. The Commission considers herein the petition for rule making filed on behalf of TLP Communications, Inc. ("petitioner") requesting the allotment of FM Channel 260A to Ketchikan, Alaska, as that community's third local FM broadcast service. Petitioner stated its intention to apply for Channel 260A if it is allotted to Ketchikan, and if authorized, to construct a station promptly, as required by the Commission in the Appendix to the *Notice*.

2. We believe the public interest would be served by proposing the allotment of Channel 260A to Ketchikan since it could provide a third local FM broadcast service to the community.

Technical Statement

3. A staff review of the proposal reveals that Channel 260A can be allotted to Ketchikan, Alaska, in conformity with the minimum distance separation requirements of Section 73.207(b)(1) and (2) of the Commission's Rules without a site restriction, at coordinates 55-20-30 and 131-38-48. Additionally, as Ketchikan is located within 320 kilometers (199 miles) of the United States-Canadian border, the Commission must obtain the concurrence of the Canadian government in the proposal.

4. Accordingly, we will seek comments on the proposed amendment to the FM Table of Allotments, Section 73.202(b) of the Commission's Rules, with regard to Ketchikan, Alaska, as follows:

	Channel No.	
City	Present	Proposed
Ketchikan, Alaska	290C3,294A	260A, 290C3, 294A

5. The Commission's authority to institute rule making proceedings, showings required, cut-off procedures, and filing requirements are contained in the attached Appendix and are incorporated by reference herein. In particular, we note that a showing of continuing interest is required by paragraph 2 of the Appendix before a channel will be allotted.

6. Interested parties may file comments on or before **January 19, 1995**, and reply comments on or before **February 3, 1995**, and are advised to read the Appendix for the proper procedures. Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554. Additionally, a copy of such comments should be served on the petitioner's counsel, as follows:

Lewis H. Goldman, P.C.
1850 M Street, N.W.
Suite 1080
Washington, D.C. 20036

7. The Commission has determined that the relevant provisions of the Regulatory Flexibility Act of 1980 do not apply to rule making proceedings to amend the FM Table of Allotments, Section 73.202(b) of the Commission's Rules. *See Certification that Sections 603 and 604 of the Regulatory Flexibility Act Do Not Apply to Rule Making to Amend Sections 73.202(b), and 73.606(b) of the Commission's Rules*, 46 FR 11549, February 9, 1981.

8. For further information concerning this proceeding, contact Nancy Joyner, Mass Media Bureau, (202) 634-6530. For purposes of this restricted notice and comment rule making proceeding, members of the public are advised that no *ex parte* presentations are permitted from the time the Commission adopts a Notice of Proposed Rule Making until the proceeding has been decided and such decision is no longer subject to reconsideration by the Commission or review by any court. An *ex parte* presentation is not prohibited if specifically requested by the Commission or staff for the clarification or adduction of evidence or resolution of issues in the proceeding. However, any new written information elicited from such a request or a summary of any new oral information shall be served by the person making the presentation upon the other parties to the proceeding unless the Commission specifically waives this service requirement. Any comment which has not been served on the petitioner constitutes an *ex parte* presentation and shall not be considered in the proceeding. Any reply comment which has not been served on the person(s) who filed the comment, to which the reply is directed, constitutes an *ex parte* presentation and shall not be considered in the proceeding.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

APPENDIX

1. Pursuant to authority contained in Sections 4(i), 5(c)(1),303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61 0.204(b) and 0.283 of the Commission's Rules, IT IS PROPOSED TO AMEND the FM Table of Allotments, Section 73.202(b) of the Commission's Rules and Regulations, as set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached.

2. *Showings Required.* Comments are invited on the proposal(s) discussed in the *Notice of Proposed Rule Making* to which this Appendix is attached. Proponent(s) will be expected to answer whatever questions are presented in initial comments. The proponent of a proposed allotment is also expected to file comments even if it only resubmits or incorporates by reference its former pleadings. It should also restate its present intention to apply for the channel if it is allotted and, if authorized, to build a station promptly. Failure to file may lead to denial of the request.

3. *Cut-off Procedures.* The following procedures will govern the consideration of filings in this proceeding.

(a) Counterproposals advanced in this proceeding itself will be considered if advanced in initial comments, so that parties may comment on them in reply comments. They will not be considered if advanced in reply comments. *(See* Section 1.420(d) of the Commission's Rules.)

(b) With respect to petitions for rule making which conflict with the proposal(s) in this *Notice,* they will be considered as comments in the proceeding, and Public Notice to this effect will be given as long as they are filed before the date for filing initial comments herein. If they are filed later than that, they will not be considered in connection with the decision in this docket.

(c) The filing of a counterproposal may lead the Commission to allot a different channel than was requested for any of the communities involved.

4. *Comments and Reply Comments; Service.* Pursuant to applicable procedures set out in Sections 1.415 and 1.420 of the Commission's Rules and Regulations, interested parties may file comments and reply comments on or before the dates set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached. All submissions by parties to this proceeding or by persons acting on behalf of such parties must be made in written comments, reply comments, or other appropriate pleadings. Comments shall be served on the petitioner by the person filing the comments. Reply comments shall be served on the person(s) who filed comments to which the reply is directed. Such comments and reply comments shall be accompanied by a certificate of service. *(See* Section 1.420(a), (b) and (c) of the Commission's Rules.) Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554.

5. *Number of Copies.* In accordance with the provisions of Section 1.420 of the Commission's Rules and Regulations, an original and four copies of all comments, reply comments, pleadings, briefs, or other documents shall be furnished the Commission.

6. *Public Inspection of Filings.* All filings made in this proceeding will be available for examination by interested parties during regular business hours in the Commission's Public Reference Room at its headquarters, 1919 M Street N.W., Washington, D.C.

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-137

In the Matter of

Amendment of Section 73.202(b) RM-8532
Table of Allotments,
FM Broadcast Stations.
(Romney, West Virginia)

NOTICE OF PROPOSED RULE MAKING

Adopted: November 21, 1994; Released: November 29, 1994

Comment Date: January 19, 1995
Reply Comment Date: February 3, 1995

By the Acting Chief, Allocations Branch:

1. The Commission has before it the petition for rule making filed by The Virginia Schools for the Deaf and the Blind ("petitioner"), licensee of Station WJGF(FM), Channel 201A, Romney, West Virginia, proposing the substitution of Channel 281A for Channel 201A at Romney. Petitioner also requests that Channel 281A be reserved for noncommercial educational use, and that Station WJGF(FM)'s license be modified accordingly. Petitioner states its intention to apply for the channel, if allotted.[1]

2. In support of its proposal, petitioner states that the substitution of Channel 281A for Channel 201A at Romney will eliminate interference with Station WJAC-TV, Channel 6, Johnstown, Pennsylvania. Petitioner also claims that there are no channels available on the noncommercial educational band.

3. Generally, noncommercial educational stations operate within the reserved portion of the FM band (Channels 201-220). However, exceptions have been made where channels in the noncommercial educational band are not available because of foreign allotments (Canadian or Mexican), or potential interference to operation on VHF Television Channel 6. Here, potential interference to Station WJAC-TV, Channel 6, Johnstown, Pennsylvania, appears to justify the reservation of a channel in the nonreserved band (Channels 221-300) for noncommercial educational use. An engineering analysis has confirmed that there are no Class A channels available in the noncommercial educational band. Therefore, the allotment and reservation of a commercial channel appears to be the only way to provide a full Class A noncommercial educational channel to Romney.

4. We believe the public interest would be served by proposing the substitution of Channel *281A for Channel 201A at Romney, West Virginia, and its reservation for noncommercial educational use. *See Rochester, Minnesota and Clear Lake and Osage, Iowa*, 7 FCC Rcd 6505 (1992). An engineering analysis has determined that Channel *281A can be allotted to Romney in compliance with the Commission's minimum distance separation requirements with a site restriction of 2.7 kilometers (1.7 miles) north at petitioner's requested site.[2] We shall also propose to modify the license of Station WJGF(FM) to specify operation on Channel *281A in lieu of Channel *201A at Romney in accordance with the Commission's Rules. In the event there are other expressions of interest for a Class A channel in the community, petitioner has indicated that there is another equivalent channel available.

5. Accordingly, we seek comments on the proposed amendment of the FM Table of Allotments, Section 73.202(b) of the Commission's Rules, for the community listed below, to read as follows:

	Channel No.	
City	Present	Proposed
Romney, West Virginia	261A	261A, *281A

6. The Commission's authority to institute rule making proceedings, showings required, cut-off procedures, and filing requirements are contained in the attached Appendix and are incorporated by reference herein. In particular, we note that a showing of continuing interest is required by paragraph 2 of the Appendix before a channel will be allotted.

7. Interested parties may file comments on or before **January 19, 1995**, and reply comments on or before **February 3, 1995**, and are advised to read the Appendix for the proper procedures. Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554. Additionally, a copy of such comments should be served on the petitioner, or its counsel or consultant, as follows:

Max D. Carpenter, Superintendent
The West Virginia Schools for the Deaf
and the Blind
301 East Main Street
Romney, West Virginia 26757 (Petitioner)

[1] Although the petitioner's request was signed, it failed to include an affidavit verifying that the statements contained in the petition were accurate to the best of its knowledge. Section 1.52 of the Commission's Rules requires that the original of any document filed with the Commission by a party not represented by counsel be signed and verified by the party and his/her address stated. In the absence of such verification, the petition may be dismissed. Section 1.401(b) of the Commission's Rules concerning rule making proceedings places petitioners on notice that their proposal must conform with the requirements of Section 1.52 regarding subscription and verification. *See also Amendment of Sections 1.420 and 73.3584 of the Commission's Rules Concerning Abuses of the Commission's Processes*, 5 FCC Rcd 3911, 3919 n.41 (1990). The petitioner is requested to rectify this omission in its comments.

[2] The coordinates for Channel *281A at Romney are North Latitude 39-22-00 and West Longitude 78-44-50.

8. The Commission has determined that the relevant provisions of the Regulatory Flexibility Act of 1980 do not apply to rule making proceedings to amend the FM Table of Allotments, Section 73.202(b) of the Commission's Rules. *See Certification That Sections 603 and 604 of the Regulatory Flexibility Act Do Not Apply to Rule Making to Amend Sections 73.202(b), 73.504 and 73.606(b) of the Commission's Rules,* 46 FR 11549, February 9, 1981.

9. For further information concerning this proceeding, contact Sharon P. McDonald, Mass Media Bureau, (202) 634-6530. For purposes of this restricted notice and comment rule making proceeding, members of the public are advised that no *ex parte* presentations are permitted from the time the Commission adopts a Notice of Proposed Rule Making until the proceeding has been decided and such decision is no longer subject to reconsideration by the Commission or review by any court. An *ex parte* presentation is not prohibited if specifically requested by the Commission or staff for the clarification or adduction of evidence or resolution of issues in the proceeding. However, any new written information elicited from such a request or a summary of any new oral information shall be served by the person making the presentation upon the other parties to the proceeding unless the Commission specifically waives this service requirement. Any comment which has not been served on the petitioner constitutes an *ex parte* presentation and shall not be considered in the proceeding. Any reply comment which has not been served on the person(s) who filed the comment, to which the reply is directed, constitutes an *ex parte* presentation and shall not be considered in the proceeding.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

APPENDIX

1. Pursuant to authority found in Sections 4(i), 5(c)(1),303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61 0.204(b) and 0.283 of the Commission's Rules, IT IS PROPOSED TO AMEND the FM Table of Allotments, Section 73.202(b) of the Commission's Rules and Regulations, as set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached.

2. *Showings Required.* Comments are invited on the proposal(s) discussed in the *Notice of Proposed Rule Making* to which this Appendix is attached. Proponent(s) will be expected to answer whatever questions are presented in initial comments. The proponent of a proposed allotment is also expected to file comments even if it only resubmits or incorporates by reference its former pleadings. It should also restate its present intention to apply for the channel if it is allotted and, if authorized, to build a station promptly. Failure to file may lead to denial of the request.

3. *Cut-off Procedures.* The following procedures will govern the consideration of filings in this proceeding.

(a) Counterproposals advanced in this proceeding itself will be considered if advanced in initial comments, so that parties may comment on them in reply comments. They will not be considered if advanced in reply comments. *(See* Section 1.420(d) of the Commission's Rules.)

(b) With respect to petitions for rule making which conflict with the proposal(s) in this *Notice,* they will be considered as comments in the proceeding, and Public Notice to this effect will be given as long as they are filed before the date for filing initial comments herein. If they are filed later than that, they will not be considered in connection with the decision in this docket.

(c) The filing of a counterproposal may lead the Commission to allot a different channel than was requested for any of the communities involved.

4. *Comments and Reply Comments; Service.* Pursuant to applicable procedures set out in Sections 1.415 and 1.420 of the Commission's Rules and Regulations, interested parties may file comments and reply comments on or before the dates set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached. All submissions by parties to this proceeding or by persons acting on behalf of such parties must be made in written comments, reply comments, or other appropriate pleadings. Comments shall be served on the petitioner by the person filing the comments. Reply comments shall be served on the person(s) who filed comments to which the reply is directed. Such comments and reply comments shall be accompanied by a certificate of service. *(See* Section 1.420(a), (b) and (c) of the Commission's Rules.) Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554.

5. *Number of Copies.* In accordance with the provisions of Section 1.420 of the Commission's Rules and Regulations, an original and four copies of all comments, reply comments, pleadings, briefs, or other documents shall be furnished the Commission.

6. *Public Inspection of Filings.* All filings made in this proceeding will be available for examination by interested parties during regular business hours in the Commission's Public Reference Room at its headquarters, 1919 M Street N.W., Washington, D.C.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

SBC MEDIA VENTURES, INC.

Appeal of Local
Rate Order of Montgomery
County, Maryland

CONSOLIDATED ORDER

Adopted: November 9, 1994; Released: November 22, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. By this Order, the Commission consolidates three related proceedings into one proceeding and rules on the merits raised in each proceeding. Specifically, the Commission resolves the appeal filed by SBC Media Ventures, Inc. ("SBC-MV") of the local rate order adopted by Montgomery County, Maryland ("the County"). The Commission also rules on the issues raised in a Motion for Declaratory Ruling filed by Montgomery County, and in third-party pleadings filed by William J. Franklin, a resident of Montgomery County, a subscriber to SBC-MV's cable television service and a participant in the local ratemaking process. In deciding this appeal, the Commission has reviewed all the pertinent pleadings filed in each of the separate proceedings. In the interest of administrative efficiency, the Commission has decided that each of the proceedings is sufficiently related to one another to justify the joint resolution of all the issues raised by each of the concerned parties in one consolidated proceeding.

2. SBC-MV, the franchisee in the above-referenced proceeding, filed with the Commission on May 24, 1994 a Petition for Review ("appeal") of the local Rate Order adopted by Montgomery County on April 29, 1994. In its Rate Order, Montgomery County established rates for basic tier service and associated equipment and installations and required SBC-MV to implement approximately $21 million in subscriber refunds.[1] In its appeal, SBC-MV does not challenge the legal basis for approximately $10 million of its $21 million total refund liability. Therefore, as explained in its appeal, SBC-MV is seeking only a partial review of Montgomery County's Rate Order, involving $11 million in subscriber refunds and associated rate reductions. On June 23, 1994, after considering a petition for stay filed by SBC-MV and an opposition to petition for stay filed by the County, the Commission granted a partial stay of the County's local Rate Order pending review on appeal.[2]

3. Montgomery County's Rate Order is effectively divided into two parts. The first part addresses an alleged "rate discrimination" violation and is disputed by SBC-MV. This part of the order accounts for $10 million in refund liability, all of which is disputed by SBC-MV. The second part of the order involves the County's ruling on the FCC Form 393[3] that SBC-MV filed with the County to determine its basic rates. This part of the order accounts for $11 million in refund liability. SBC-MV challenges only a portion of this $11 million liability, accounting for approximately $1 million in potential refunds. On June 8, 1994, Montgomery County filed an Opposition to Petition for Review, urging the Commission to reject SBC-MV's appeal and to allow Montgomery County's Rate Order to go into effect unchanged.[4] Specifically, Montgomery County argues that the disputed portion of the Rate Order covering the rate discrimination issue should not be the subject of the appeal because the question of its legality is already before the Commission in a separate proceeding.[5] Montgomery County asserts that the other portions of the Rate Order to which SBC-MV objects have a reasonable basis and do not merit Commission reversal on appeal.[6]

4. Under the Commission's rules, appeals of franchising authorities' local rate orders are reviewed by the Commis-

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[1] Under the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act"), and the Commission's implementing regulations, local franchising authorities may regulate rates for basic cable service and associated equipment. *See* Cable Television Consumer Protection and Competition Act, Pub. L. No. 102-385, 106 Stat. 1460 (1992); Communications Act, § 623(b), 47 U.S.C. § 543(b).

[2] *Order* (Petition for Stay of Local Rate Order of Montgomery County), DA 94-702 (released June 23, 1994).

[3] The Commission's Form 393 ("Determination of Maximum Initial Permitted Rates for Regulated Cable Programming Services and Equipment") directs a cable operator to determine its maximum permitted rates for regulated service, equipment, and installations.

[4] Mr. William Franklin, a resident of Montgomery County, who has participated in the County's ratemaking process also filed a Petition for Partial Review of the County's Rate Order on May 31, 1994. Both the County and SBC-MV have opposed Mr. Franklin's petition in separately filed pleadings. Mr. Franklin filed a Reply to Oppositions to Petition for Partial Review with the Commission on June 30, 1994.

[5] On May 18, 1994, Montgomery County filed with the Commission a Motion for Declaratory Ruling requesting that the Commission rule on the propriety, under federal law, of its prescribed remedy for SBC-MV's alleged rate discrimination violation. On June 2, 1994, SBC-MV filed an Opposition to the Motion for Declaratory Ruling. Mr. Franklin also filed Comments on the Motion for Declaratory Ruling on June 2, 1994.

[6] In his Petition for Partial Review, Mr. Franklin alleges that SBC-MV has provided a cable guide publication to subscribers since November 1993 in violation of the 1992 Cable Act's negative-option billing provision. Because the County did not address this issue in its Rate Order, this appeal of the County's Rate Order is not the proper forum for the resolution of this issue. Furthermore, under the Commission's rules, the County was not required to resolve and did not choose to resolve this issue in its Rate Order. The negative option billing provision governs the circumstances under which a cable operator may bill a subscriber for a particular service, rather than the reasonableness of the actual rate charged a subscriber for that service. *Third Order on Reconsideration in MM Docket 92-266* at ¶ 128 (released March 30, 1994) (*"Third Recon. Order"*). Mr. Franklin may request that the County or the Commission initiate an inquiry into SBC-MV's billing practices, but to ensure the swiftest implementation of reasonable rates, this inquiry should be conducted separately from the ratemaking process. The ne-

sion.[7] In ruling on appeals of local rate orders, the Commission will not conduct a *de novo* review, but instead will sustain the franchising authority's decision as long as there is a reasonablebasis for that decision.[8] Therefore, the Commission will reverse a franchising authority's decision only if we determine that the franchising authority acted unreasonably in applying the Commission's rules in rendering its local rate order.[9] If the Commission reverses a franchising authority's decision, it will not substitute its own decision, but instead it will remand the issue to the franchising authority with instructions for its resolution.[10]

II. RATE DISCRIMINATION

A. Background

5. The principal dispute arising from Montgomery County's Rate Order involves the County's determination that SBC-MV has engaged in rate discrimination in violation of local law and the 1992 Cable Act. To remedy this alleged violation, the County has ordered $10 million in subscriber refunds. SBC-MV claims that to prevent its customers who only subscribe to the basic tier from experiencing dramatic rate increases within a nine-month time span from December 31, 1992 until September 1, 1993, SBC-MV capped this class of subscribers' rates at their then-existing levels, while increasing the basic service rate for all other subscribers. Therefore, basic-only subscribers who became customers on or before December 31, 1992 were grandfathered at the 1992 basic rate of $6.95 per month (exclusive of franchise fees); basic-only subscribers who became customers between January 1, 1993 and August 31, 1993 were grandfathered at the rate of $10.00 per month (exclusive of franchise fees); and all subsequent subscribers to SBC-MV's services were charged $13.95 per month (exclusive of franchise fees) for basic service. Any grandfathered basic-only subscriber ceased to receive the grandfathered rate for the basic tier if he or she upgraded service. Therefore, the number of grandfathered subscribers could not increase and was continually decreasing as those subscribers upgraded service. Due to the grandfathering, as of September 1, 1993 (the implementation date for the Commission's rate regulations), SBC-MV was offering basic tier service to three separate classes of subscribers at three different rates. SBC-MV claims that, as of September 1, 1993, less than 4 percent of its subscribers were being charged either the $6.95 rate or the $10.00 rate for the basic service tier, while over 96 percent of its subscribers were charged the highest rate for the basic tier.

6. In its Rate Order, the County held that this practice of subscriber classification constituted rate discrimination in violation of its local Cable Communications Law[11] and in violation of two provisions of the 1992 Cable Act.[12] In the absence of federal legislative or administrative guidance, the County relied on local law to craft its own remedy and, accordingly, ordered SBC-MV to refund to its subscribers the difference between the higher basic rate charged to both its multi-package and post-September 1, 1993 basic-only subscribers and the lowest rate of $6.95 charged to its grandfathered basic-only subscribers. This portion of the Rate Order totals approximately $10 million in potential subscriber refunds. Under the terms of the County's Rate Order, SBC-MV's refund liability would run from September 1, 1993 until the day that it implemented uniform basic tier rates.[13] SBC-MV argues that its decision to grandfather a segment of its basic-only subscribers at their then-existing rates, during the time that it increased the rates for the rest of its subscribers, was a legitimate business decision that does not violate the requirement that rates be uniform throughout the franchise area or constitute any other type of illegal discrimination prohibited under the 1992 Cable Act. Specifically, SBC-MV asserts that this grandfathered rate structure was intended to ameliorate the impact of rate restructuring undertaken to comply with the terms of the 1992 Cable Act. In the alternative, SBC-MV argues that even if the grandfathered rates were found to violate the 1992 Cable Act, the appropriate remedy would be a "cease and desist" order, not an order prescribing subscriber refunds. Conversely, the County asserts that an order requiring subscriber refunds is the County's best available remedy because refunds directly impact those subscribers who have been harmed by SBC-MV's alleged "rate discrimination" and prevent SBC-MV from benefitting from its purportedly illegal actions. The County found that SBC-MV offered no reasonable justification for its rate classification scheme. The County argues that, although the appropriate remedy for rate discrimination is uncertain under federal law, the County has the authority under local law to order subscriber refunds to remedy a finding of rate discrimination.[14] The County also urges the Commission to reject SBC-MV's appeal with respect to the rate discrimination issue on the grounds that the issue should be resolved in a bifurcated proceeding initiated by the

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cessity for a separate inquiry is compounded by the fact that since the County has made no inquiry on the issue, there is no factual record or statement of findings from which the Commission could base a decision on appeal. Therefore, the Commission dismisses this issue from further consideration in this appeal. Mr. Franklin is free to pursue this matter in a separate proceeding brought before his state or local government or before the Commission. *See Id.* at ¶ ¶ 122-131. We also note here that Mr. Franklin seeks reconsideration of our decision, released June 23, 1994, granting a partial stay pending review of the County's local Rate Order. That reconsideration petition, which was filed on June 27, 1994, is rendered moot by this decision on the merits.

[7] 47 C.F.R. § 76.944.

[8] *See Report and Order and Further Notice of Proposed Rulemaking in MM Docket 92-266,* 8 FCC Rcd 5631, ¶ 149 (released May 3, 1993) (*"Report and Order"*); *Third Recon. Order* ¶ 81.

[9] *Id.*

[10] *Id.*

[11] *See* Montgomery County Code 1984, as amended, chapter 8A, Cable Communications Law §§ 8A-15(a) (nondiscrimination), 8A-20(a)(3) (remedies), ("[A] franchisee must not... grant undue preferences or advantages to any subscriber..., must have a uniform rate structure..., [and] must not... discriminate against subscribers...")

[12] *See infrao* footnotes 16 and 17.

[13] SBC-MV asserts in its appeal that, upon receipt of the County's Rate Order, it announced on May 18, 1994 the end of its three classes of basic tier rates, effective 30 days therefrom, after which all subscriber classes would be charged the rate of $13.95 for the basic service tier.

[14] *See suprao* footnote 11.

County as a Motion for Declaratory Ruling[15] and reviewed separately from the other issues raised in the appeal. The County seeks the Commission's approval of its proposed remedy to impose subscriber refunds, which it argues are authorized under federal law. As explained in detail below, we will remand this portion of the rate order back to the County with the instruction that the County follow the guidelines laid out in this decision in rendering its determination.

B. Discussion

7. In the interest of administrative efficiency, the Commission has decided to consolidate the resolution of the rate discrimination issue raised in the County's Motion for Declaratory Ruling with the resolution of this appeal of the County's Rate Order. In so doing, the Commission has been careful to consider all the arguments made on this issue by all sides in the submissions filed in both proceedings before us.

8. The County alleges that SBC-MV's rate classification scheme purportedly violates two separate provisions of the 1992 Cable Act. First, under Section 623(d) of the Communications Act and Section 76.984 of the Commission's rules, cable operators must offer a rate structure that is uniform throughout the franchise area.[16] Secondly, under Section 623(e) of the Communications Act and Section 76.983 of the Commission's rules, regulatory authorities, including franchising authorities, may prohibit cable operators from engaging in discrimination among subscribers.[17] The 1992 Cable Act seeks to ensure that rates are uniform throughout the franchise area, so that no group of subscribers within a franchise area is required to pay more for the same service than another group. Although the legislative history suggests that Section 623(d), which requires geographic uniformity, is intended, in part, to prevent cable operators from pricing service according to income level and from undercutting potential competitors by offering lower rates only in areas where competitors seek to offer a competing service,[18] the provision must also be given its plain meaning. On its face, the provision requires the same rates for the same service within a geographic area. Therefore, SBC-MV's argument that this provision merely prevents rate classification schemes based solely on geography or neighborhood does not give the provision its proper scope. SBC-MV's offering of three separate rates for the same basic service tier to three different groups of subscribers in the same geographic area resulted in a basic tier rate structure that was not uniform throughout the franchise area.[19]

9. The 1992 Cable Act and the Commission's implementing rules specifically contemplate certain exceptions to the fundamental requirement of uniformity.[20] The Commission has noted several specific instances where an operator may be justified in offering different rates for the same service to specific, reasonable categories of subscribers:

> The Act specifically mandates a uniform "rate structure." The legislative history does not reveal any congressional intent to mandate a uniform rate for all services and classes of customers. Indeed, Section 623(e) specifically contemplates [that] special categories of customers may receive separate rates. [footnote omitted] Accordingly, we conclude that Section 623(d) does not preclude establishment of reasonable categories of customers and service by cable operators. Thus, for example, as suggested in the *Notice*, we do not believe that Congress intended a *per se* prohibition on differences in rates between seasonal and full-time subscribers. We also find that uniform, non-predatory bulk discounts to multiple dwelling units, including apartment buildings, hotels, condominium associations, hospitals, universities, and trailer parks, could form a valid basis for distinctions among subscribers. Introductory or promotional rates universally applied at a given time but subsequently discontinued would also not be prohibited. And, as is suggested by Section 623(e), discussed further below, reasonable discounts may be made to senior citizens or other economically disadvantaged groups and charges may be set to facilitate the reception of service by hearing impaired individuals. As we have previously discussed in our tier "buy-through" proceeding, technological differences in the service offered within a geographic area, such as might result from the staged rebuilding of a system, would also not conflict with this provision.[21]

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[15] *See supra* footnote 5.

[16] This provision of the 1992 Cable Act specifically states that, "A cable operator shall have a rate structure, for the provision of cable service, that is uniform throughout the geographic area in which cable service is provided over its cable system." Cable Television Consumer Protection and Competition Act, Pub. L. No. 102-385, 106 Stat. 1460 (1992); Communications Act, § 623(d); 47 U.S.C. § 543(d). Section 76.984(a) of the Commission's rules states that, "The rates charged by cable operators subject to §§ 76.922 and 76.923 shall be provided pursuant to a rate structure that is uniform throughout each franchise area, in which cable service is provided." Section 76.984(b) goes on to state that, "This section does not prohibit the establishment by cable operators of reasonable categories of service and customers with separate rates and terms and conditions of service, within a franchise area."

[17] This provision of the 1992 Cable Act specifically states that, "Nothing in this title shall be construed as prohibiting any Federal agency, State, or a franchising authority from -- (1) prohibiting discrimination among subscribers and potential subscribers to cable service, except that no Federal agency, State, or franchising authority may prohibit a cable operator from offering reasonable discounts to senior citizens or other economically disadvantaged group discounts; or (2) requiring and regulating the installation or rental of equipment which facilitates the reception of cable service by hearing impaired individuals." Cable Television Consumer Protection and Competition Act, Pub. L. No. 102-385, 106 Stat. 1460 (1992); Communications Act, § 623(e); 47 U.S.C. § 543(e).

[18] Senate Committee on Commerce, Science, and Transportation, S. Rep. No. 92, 102d Cong., 1st Sess. (1991) at 76 (". . . cable operators must offer uniform rates throughout the geographic area in which they provide cable service. This provision is intended to prevent cable operators from having different rate structures in different parts of one cable franchise. This provision is also intended to prevent cable operators from dropping the rates in one portion of a franchise area to undercut a competitor temporarily.")

[19] The Commission has interpreted "geographic area" to mean the franchise area. *See* 47 C.F.R. § 76.984; *Report and Order* at ¶ 422.

[20] *See Report and Order* at ¶ 423.

[21] *Id.*

10. Though the parties do not address the issue, it is conceivable that SBC-MV may have viewed its rate classification scheme as a promotion and, therefore, not subject to the uniformity requirement. As stated above, "[i]ntroductory or promotional rates universally applied at a given time but subsequently discontinued [are not] prohibited."[22] While the evidence before us is not sufficient to permit us to resolve whether the classification scheme constituted a promotion, SBC-MV might have sought by its scheme to preserve the subscriptions of a particularly price-sensitive segment of its subscriber base by holding down the rates for this group during a period of rate restructuring that would otherwise have resulted in significant and immediate higher prices for service.[23] Therefore, such a plan, if found to exist, could amount to a promotion.[24] However, some aspects of the scheme do not resemble a promotion. For example, a promotion, by definition, must operate only for a reasonable, finite period.[25] It cannot be determined from the facts before us whether and when the plan, when initiated, was intended to end. SBC-MV claims that the number of subscribers affected by its rate classification scheme was continually diminishing as subscribers changed service and that the scheme would have expired, eventually, under its own terms. The intervention of the local rate order caused SBC-MV to end the plan. Therefore, even if it is found to have started as an allowable promotion, at some point thereafter the rate classification plan may have ceased to be a promotion and thereby ceased to be an allowable exception to the uniformity requirement. We remand this issue to the County with instructions that it determine, consistent with the analysis here, whether SBC-MV's rate classification scheme constituted a promotion at any time and therefore an allowable exception to the uniformity provision of Section 623(d).

11. Even if the County finds that SBC-MV's rate classification scheme does not constitute a legitimate exception to the uniformity requirement of Section 623(d) and therefore violates Section 623(d), it must apply an appropriate remedy. It did not do so here. Neither the 1992 Cable Act nor the Commission's rules articulate specific remedies that an authorized regulatory body may implement in response to violations of the geographic uniformity requirement or proven instances of discrimination. Although the County could properly order SBC-MV to cease offering the rate classifications, as it did, the County could not order subscriber refunds other than those resulting from a review of a properly completed Form 393, since to do otherwise goes beyond the scope of the County's authority under the Act and the Commission's implementing regulations. The County's remedy, if it concludes that SBC-MV's rates violate Section 623(d), is to require SBC-MV to submit a revised Form 393 that accurately accounts for the number of subscribers receiving each of the three rates that it charged for the basic service tier. SBC-MV's Form 393 appears to reflect only the $13.95 rate and not the grandfathered rates.[26] In other words, SBC-MV must adjust the number of subscribers that it lists on Line 103 of Form 393 to reflect the different rates that it was actually charging for the basic tier.[27] Those subscribers who paid a grandfathered rate for the basic tier should not be counted as full subscribers. Instead, those subscribers should be accounted for on Form 393 by a number that reflects the same proportional relationship that exists between the rate they were paying and the prevailing rate. For instance, a subscriber who received the grandfathered rate of $6.95 would not be included as one subscriber, but instead as 695/1395ths of a subscriber. Parts of SBC-MV's Form 393 affected by this weighted average need to be amended to reflect the change. Once it amends its Form 393, SBC-MV's revenues will no longer be overstated in the context of determining its maximum rates. The County then would be able to order refunds based on the revised Form 393 from the date the rate classification scheme was terminated by SBC-MV back to the date the County finds that the scheme ceased to be a valid promotion. No refunds may be ordered for any period in which the County may find a valid promotion existed, since such promotional rates are inherently temporary and are not to be reflected in SBC-MV's Form 393.[28]

12. No subscriber refund is available under our rules to remedy a violation of the geographic uniformity provision, other than such refunds as would result from review of an amended Form 393. Subscriber refunds, under the Commission's rules, must only be used to return the difference between unreasonable rates and reasonable rates to the subscribers; they must not be used as de facto penalties or forfeitures.[29] Although the County is correct in asserting that it has the authority to impose fines and forfeitures, such remedies are reserved, under the Commission's rules, to cure instances where a cable operator has not complied with the terms of a franchising authority's decision, such as

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[22] *Id.*

[23] SBC-MV characterizes its rate classification scheme as an effort to "ease the transition from an unregulated to a regulated environment." Petition for a Stay, 5. Whether this effort could be classified as a promotion was not addressed.

[24] The $6.95 rate was "universally applied at a given time," since it was available to all basic-only subscribers who became customers on or before December 31, 1992. The $10.00 rate was similarly "universally applied."

[25] The *Report and Order* at ¶ 423 clarifies this: "Introductory or promotional rates universally applied at a given time but *subsequently discontinued* (emphasis added) would also not be prohibited."

[26] We are unable to discern from the materials provided in the pleadings whether or not the County has required SBC-MV to make the adjustments in its Form 393. If so, SBC-MV will not be required to update its filing and will not face any more potential refund liability.

[27] *See Public Notice*, Questions and Answers Relating to FCC Form 393, Question 5 (July 30, 1993). Although this question and answer specifically dealt with the treatment of bulk discount subscribers, the same reasoning applies to this situation by analogy. Generally, Form 393 seeks to capture a cable operator's actual revenue figures and then derive its maximum permitted rates. If a cable operator does not account for its discounted rates, it would be overstating its revenues and thus deriving its maximum permitted rates from inaccurate data.

[28] If the County finds that SBC-MV's rate classification scheme never constituted a valid promotion, then the County could order refunds back to the initial date of regulation, September 1, 1993.

[29] *See Report and Order* at ¶ ¶ 142-145.

an order rolling back rates or a request for supplemental information, or where an operator has attempted to mislead the franchising authority.[30]

13. SBC-MV's attempt to grandfather the basic tier rates for certain classes of subscribers does not appear to violate, and the County has not alleged that it does violate, any federal anti-discrimination law.[31] Therefore, to the extent it wishes to seek a further remedy than that set forth in paragraphs 11 and 12 herein or to the degree it finds Section 623(d) was not violated, the County must rely on either state or local law for any finding that SBC-MV's rate classification scheme is illegal discrimination, as well as for any remedy for such alleged discrimination. The County has alleged that SBC-MV's rate classification scheme violates both a local statute and the local franchise agreement entered into between the County and SBC-MV. If local laws have been violated, the proper remedy would also have to be found under local law.[32] Because the resolution of this issue must rest with an interpretation of applicable local law and not federal law, a state or local court is the appropriate forum to hear this matter.[33]

III. HOURLY SERVICE CHARGE

A. Background

14. Upon the recommendation of its cable consultant, the County rejected SBC-MV's calculated Hourly Service Charge ("HSC") of $23.59 and prescribed an alternative HSC of $11.25. The County set the rate for SBC-MV's HSC after receiving what it believed to be an inadequate or incomplete justification for SBC-MV's own derived HSC. SBC-MV claims that the rate set by the County is impermissibly low because it falls below the $13.00 hourly rate paid to its service personnel and therefore would not even allow SBC-MV to recoup what it pays out to its employees on an hourly basis. It is the County's position that absent proof to the contrary, it was reasonable for the County to assume that SBC-MV's hourly payments for contract labor are less than its payments to its own employees and, accordingly, established an average wage of $11.25. Furthermore, the County asserts that SBC-MV repeatedly refused to provide it with additional necessary information to verify the basis for SBC-MV's own derived HSC, particularly information related to the cost and use of contract labor. SBC-MV counters that it has provided all the necessary information to the County to justify its proposed HSC and that this HSC should be accepted by the County. It appears from the pleadings that this is an issue which has perpetuated a continuing disagreement between the two parties that has lasted a number of months and has resulted in the County setting SBC-MV's HSC at a rate derived by the County's consultant, rather than at a rate based on the figures supplied on SBC-MV's Form 393.

B. Discussion

15. Generally, the Commission's rules require us to leave regulation of basic tier service to the sound discretion of the certified local franchising authorities. Although local franchising authorities have broad authority to enforce compliance with their requests for information and may prescribe rates, they must exercise this authority in accordance with the Commission's rules.[34] However, the cable operator ultimately bears the burden of proving the reasonableness of all of its regulated rates.[35] If SBC-MV's claim is accurate that the HSC adopted by the County falls below the hourly wage paid to its employees, it is possible that the County's HSC was not based upon SBC-MV's actual costs.[36] Because this outcome would contravene the intent of the 1992 Cable Act and the Commission's rules, the Commission is unable to conclude the County's HSC is reasonable, based upon the record before us. As a condition of the stay that we granted in this case, we required SBC-MV to submit to the County, within 10 days of the release of the stay order, the information regarding SBC-MV's use of contract labor that the County had previously requested.[37] Because SBC-MV has informed us that this information has been provided to the County as required,[38] we will hereby remand to the County the proper determination of SBC-MV's HSC with the instruction to the County to render a decision based on the best information available. In this instance, as in most, the best information available should be that information contained on and offered in support of a cable operator's FCC Form 393. However, because the burden to justify its rates is borne by the cable operator, it is the cable operator's duty to make sure that it complies with a franchising authority's request to provide documentation and supporting evidence to

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[30] *See* 47 C.F.R. § 76.943.

[31] The County has asserted that Section 623(e) is relevant to its determination. This provision simply seeks to ensure that the terms of the Act are not construed to prevent regulatory authorities, including franchising authorities such as the County, from prohibiting various forms of discrimination by cable operators among subscribers, while also ensuring that cable operators are still able to offer special discounted rates to senior citizens and economically disadvantaged groups.

[32] *See* 47 C.F.R. § 76.944(a) ("The Commission shall be the sole forum for appeals of decisions by franchising authorities on rates for the basic service tier or associated equipment involving whether or not a franchising authority has acted consistently with the Cable Act or §§ 76.922 and 76.923. Appeals of ratemaking decision by franchising authorities that do not depend upon determining whether a franchising authority has acted consistently with the Cable Act or §§ 76.922 or 76.923, may be heard in state or local courts.")

[33] According to the pleadings filed by SBC-MV, SBC-MV has asked a local court to rule on the propriety of the County's actions under local law.

[34] *See Order* (Petition for Stay of Local Rate Order by Century Southwest Cable Television Corp. against the City of West Hollywood), DA 94-489 at para. 8 (released May 13, 1994).

[35] *See* 47 C.F.R. § 76.937.

[36] Although the County suggests that there is good reason to assume that SBC-MV pays its contract labor less than it pays its employees, the County offers no evidence that reasonably leads to this conclusion.

[37] The County requested that SBC-MV provide the County with invoices for SBC-MV's contract labor and with a justification for the number of labor hours allocated to regulated services.

[38] In order to fulfill the requirements of the stay order, SBC-MV submitted a Stay Compliance Report with the Commission on July 22, 1994. This report indicates that SBC-MV, as required under the terms of the stay, has provided the County with the requisite contract labor invoices and a justification for its labor hour allocation, established an interest-bearing escrow account, and notified subscribers of possible refunds.

prove the reasonableness of its rates. In the event that the information submitted by SBC-MV does not fully comply with the terms of our stay order, the County is not required under either the terms of this order or under the Commission's rules to withhold a final decision on SBC-MV's HSC until the information is presented. Instead, the County may set SBC-MV's HSC based on the best information available at the time.[39]

IV. A/B SWITCHES

A. Background

16. The County set a rate of $3.00 per switch for the sale of A/B switches to subscribers by SBC-MV. SBC-MV had previously been charging $10.00 for each switch. SBC-MV claims that A/B switches are not items properly subject to regulation by the County because they are used by subscribers only to receive off-the-air broadcast signals and not used for the reception of basic tier service. The County contends, however, that SBC-MV has not borne its burden of proving that A/B switches are not used for the reception of basic tier service. The County also asserts that the price it has set for A/B switches is in line with the market price for A/B switches offered by other vendors in the community.

B. Discussion

17. Under the Commission's rules, rates for equipment that is used to receive basic tier service and that is offered for sale by cable operators are regulated.[40] Regulated equipment ". . . consists of all the equipment in a subscriber's home that is used to receive the basic tier. . . . Such equipment shall include, but is not limited to: (1) converter boxes; (2) remote control units; (3) connections for additional television receivers; and (4) other cable home wiring."[41] This list of equipment is not intended to be an exhaustive list of all possible types of regulated equipment, but all such equipment, at a minimum, "must be used to receive the basic service tier." While the Commission has interpreted the phrase "equipment used to receive the basic service tier" broadly so as to comport with Congressional intent,[42] the switches at issue are simply not used to receive cable service. A/B switches are used by subscribers to switch off cable service and to receive, instead, off-the-air broadcast signals. The switches are used only by cable subscribers who choose not to watch cable programming. We note also that the switches are available from other sources in the County. In fact, the County prescribed a rate for sale of A/B switches by SBC-MV that was representative of the prices offered for such switches by other vendors in the community. So, not only are the A/B switches not "used to receive the basic service tier," but competitive sources for such switches exist in the community through which subscribers may obtain them. Accordingly, we conclude the County's determination that A/B switches constitute regulated equipment is unreasonable and we remand the County's decision regarding the regulation of A/B switches for further proceedings consistent with this ruling.

V. PEG ACCESS FEE

A. Background

18. Under the terms of its franchise agreement, SBC-MV is required to charge an additional fee to subscribers that is used to support channels designated for public, educational and governmental purposes (i.e., PEG channels). According to SBC-MV, SBC-MV's 1.5 percent PEG access fee was not accounted for as an internal cost (i.e., included in the per channel rates derived in Worksheets 1 and 2 of FCC Form 393) in deriving its maximum permitted rate for basic tier service. SBC-MV claims that it did not include the PEG access fee in its basic rate calculations because this fee had traditionally been treated as an external cost added onto and itemized on a subscriber's bill in the same manner as the franchise fee. The County claims that it was unable to determine from the face of SBC-MV's FCC Form 393 whether the PEG access fee had been accounted for or not and that SBC-MV had declined to provide further clarification of the problem upon request by the County. The County's Rate Order also did not explicitly account for the inclusion of this fee as either an internal cost or as an allowable external cost. It is the County's position that if SBC-MV can demonstrate that it did not include the PEG access fee in the per channel rates derived in Worksheets 1 and 2 of FCC Form 393, then the County will recalculate SBC-MV's permitted rate based on the corrected numbers and extend SBC-MV's time for compliance accordingly, assuming this can be done without affecting the one-year limit on subscriber refunds.

B. Discussion

19. A cable operator's permitted per channel charges for regulated programming services may be adjusted for changes in external costs.[43] Our regulations provide that the operator may adjust its charges to the extent that certain external cost increases exceed the rate of inflation. However, except in the case of franchise fees, the operator should include these external costs in its initial rate calculations on FCC Form 393. Franchise fees are the only external costs that should not be included in programming revenue when calculating an operator's initial permitted rates. PEG access fees and external costs other than franchise fees should be included in the per channel rates calculated in Worksheets 1 and 2 of a cable operator's FCC Form 393.[44] Thereafter, any future changes in external costs greater than the rate of inflation should be allowed as adjustments to an operator's permitted charges. Adjustments to SBC-MV's permitted charges should be made according to the Commission's rules for the treatment of external costs.[45] Therefore, SBC-MV should be allowed to account for its PEG access fee as an internal cost in setting its initial regulated programming rates. The County has explicitly offered to allow SBC-MV to resubmit for approval a revised FCC Form 393 that includes a PEG access fee allocation. Because the County will allow this resubmission, we remand this issue to the County for final

39 *See Third Recon. Order* at ¶ 84.
40 47 C.F.R. § 76.923(i).
41 47 C.F.R. § 76.932(a).
42 *See Report and Order* at ¶ 283.
43 47 C.F.R. § 76.922(d)(3).
44 47 C.F.R. § 76.922(d)(3)(iv)(C).
45 *See* 47 C.F.R. § 76.922(d).

resolution on the condition that SBC-MV make every effort to provide this revised filing to the County as expeditiously as possible.

VI. BULK BASIC RATES

A. Background

20. The County has ordered SBC-MV to justify all of the various bulk basic rates that it charges in the area.[46] The County has forewarned SBC-MV that in the event that the County finds any of these rates to be unreasonable it will reduce the unreasonable rates to the lowest bulk rate offered. The County claims that it has simply prescribed an appropriate and lawful remedy that it may take in the event that SBC-MV is unable to demonstrate that its current bulk rates are either grandfathered or otherwise justified under the Commission's rules. If SBC-MV can demonstrate that its bulk rates are lawful, the County will release SBC-MV from refund liability for these bulk rates. It is SBC-MV's position that this review is unnecessary, for, irrespective of grandfathered rates already in place, it may negotiate new bulk rates as long as these new rates are uniform among Multiple Dwelling Units ("MDUs") of similar size and for contracts of similar duration.

B. Discussion

21. Franchising authorities have the authority to regulate bulk basic rates to ensure compliance with the uniform rate provisions of the 1992 Cable Act.[47] In its Rate Order, the County informed SBC-MV of its intention to regulate its bulk basic rates, the standards of review it will use, and the prospective remedy for nonconformance. The County has asked SBC-MV to provide it with information that would allow the County to make a determination regarding the reasonableness of SBC-MV's bulk rates, but it has not ordered SBC-MV to modify any those rates. Although the County has not yet acted on SBC-MV's various bulk discounts, any 8action the County does take must comport with our rules.[48] Under our rules, cable operators may offer different bulk rates to MDUs of different sizes and may vary bulk rates based on the duration of the contracts, provided the operator can justify the rate differences based on relative cost savings.[49] Operators must, however, offer the same rates to MDUs of the same size with contracts of similar duration.[50] Accordingly, the County may order the rates of an MDU reduced to a lower rate established by the operator for an MDU of the same size under the same conditions. The County may not, however, simply reduce all bulk rates offered by SBC-MV to the lowest bulk rate. In the event the County renders a particular decision regarding SBC-MV's bulk discounts that SBC-MV believes is unreasonable, SBC-MV will have the opportunity to appeal that decision to the Commission at the proper time. Therefore, since a decision by the Commission on this issue at this time would be premature, we remand this issue to the County for further disposition.

22. Accordingly, IT IS ORDERED that all of the issues raised in the following proceedings: (1) the appeal by SBC Media Ventures, Inc. of the local Rate Order adopted by Montgomery County, Maryland; (2) the Motion for Declaratory Ruling filed by Montgomery County; and (3) the pleadings regarding the County's Rate Order filed by Mr. William J. Franklin, a resident of Montgomery County, a subscriber to SBC-MV's cable television service and a participant in the local ratemaking process, are consolidated into one proceeding.

23. IT IS FURTHER ORDERED that the appeal filed by SBC Media Ventures, Inc. IS REMANDED.

24. IT IS FURTHER ORDERED that the provision of Montgomery County's Rate Order governing rate discrimination IS REMANDED to the local franchising authority for further proceedings consistent with this opinion. IT IS FURTHER ORDERED that the provision of Montgomery County's Rate Order governing SBC Media Ventures' regulated hourly service charge IS REMANDED to the local franchising authority for further proceedings consistent with this opinion. IT IS FURTHER ORDERED that the provision of Montgomery County's Rate Order regarding A/B switches IS REMANDED to the local franchising authority for further proceedings consistent with this opinion. IT IS FURTHER ORDERED that Montgomery County's Rate Order regarding PEG access fees IS REMANDED to the local franchising authority for further proceedings consistent with this opinion. IT IS FURTHER ORDERED that Montgomery County's Rate Order regarding bulk rate discounts IS REMANDED to the local franchising authority for further proceedings consistent with this opinion.

25. IT IS FURTHER ORDERED that the Franklin Petition for Partial Review with regard to the negative-option billing issue IS DENIED. IT IS FURTHER ORDERED that the Franklin Petition for Partial Review with regard to the rate discrimination issue IS DENIED.

26. This action is taken by the Chief, Cable Services Bureau, pursuant to authority delegated by Section 0.321 of the Commission's rules. 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

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[46] Bulk basic rates are discounted service rates offered to multiple dwelling units, such as apartment buildings and condominiums.

[47] *Report and Order* at ¶ 425.

[48] 47 C.F.R. § 76.984. *See also Report and Order* at ¶ ¶ 421-425; *Third Recon. Order* at ¶ ¶ 18-24.

[49] *Id.*

[50] *Id.*

Before the
Federal Communications Commission
Washington, D.C. 20554

PUBLIC NOTICE

Released: November 21, 1994

US/CANADA INTERIM SHARING ARRANGEMENT FOR 2 GHz BROADBAND PCS

On November 14, 1994, representatives of the FCC and Industry Canada concluded a sharing arrangement for 2 GHz Broadband Personal Communications Services (PCS). This interim sharing arrangement provides for use of the 1850-1990 MHz band for PCS along the United States and Canada border. This sharing arrangement should assist parties intending to participate in the FCC auction process and should facilitate the eventual provision of PCS services along the border.

The principal provisions of this interim sharing arrangement are:

- The frequency band 1850-1990 MHz is to be shared on an equal basis and both countries are to have full use of these frequencies for the provision of PCS services.
- Additional use of the 1850-1990 MHz frequency band for fixed point-to-point microwave use is to be limited and discouraged and any new use of the 1910-1930 MHz band for fixed microwave operations is to be avoided. (The 1910-1930 MHz portion of the 1850-1990 MHz band has been designated for unlicensed PCS use in the United States and a similar type of use in Canada.)
- Any new PCS use of these frequencies is not to cause harmful interference to existing fixed point-to-point microwave operations in the other country.
- Coordination of all PCS systems within 120 km (75 miles) of the border is required and will be based on:

  - A technical analysis, using recognized industry procedures such as TIA/EIA Bulletin (TSB10-F), that interference is not caused to existing microwave operations; or, alternatively,

  - A mutually acceptable arrangement between the PCS and fixed microwave operators.

- Licenses for PCS base station facilities within 72 km (45 miles) of the border will be conditioned to indicate that future coordination is required between PCS operators in both countries to ensure that interference is not caused to PCS operations in the other country and that the band is shared on an equal basis. (This is similar to actions taken during the initial licensing of the cellular radio service.)
- The predicted or measured median field strength of any PCS base station is not to exceed 47 dBuV/m at any location at or beyond the border unless the affected PCS operators in the adjacent areas agree.
- Compatible PCS operations at the border are best assured through coordination of operating and technical parameters by PCS operators; and, PCS operators are to notify the FCC and Industry Canada of any agreements. Such agreements are subject to review by the Agencies.

The full text of the arrangement has been placed in GEN Docket No. 90-314 and copies are available from International Transcription Service at (202) 857-3800. For further information, contact Tom Mooring or Rod Small in the Office of Engineering and Technology at (202) 653-8114 (6) or Henry Straube in the International Bureau at (202) 254-3394.

FEDERAL COMMUNICATIONS COMMISSION

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 91-140

In re

Revision of RM-8414
Radio Rules and Policies

SECOND MEMORANDUM OPINION AND ORDER

Adopted: October 20, 1994; Released: November 8, 1994

By the Commission: Commissioner Barrett issuing a separate statement.

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I. INTRODUCTION

1. This *Order* disposes of petitions for reconsideration of the *Memorandum Opinion and Order and Further Notice of Proposed Rule Making* in MM Docket No. 91-140, 7 FCC Rcd 6387 (1992) (hereinafter *First Reconsideration Order),* which revised the Commission's rules governing the ownership of interests in multiple radio stations.[1] In the *First Reconsideration Order,* the Commission revised Section 73.3555 of the Commission's Rules (47 C.F.R. § 73.3555) to increase the national radio ownership limit from 12 AM and 12 FM stations to 18 AM and 18 FM stations, and ultimately to 20 AM and 20 FM stations.[2] The Commission also revised the national minority ownership cap, which had permitted non-minority owners to take a non-controlling interest in an additional two AM and two FM stations that were minority-controlled, and permitted minority owners to own an additional two stations outright (*i.e.,* 14 AM and 14 FM stations). The *First Reconsideration Order* modified the rule to permit all owners to take a non-controlling interest in an additional three stations per service above the national caps if those stations were controlled by minorities or small businesses. It declined to adopt a provision allowing minority broadcasters to own more stations outright.

2. The *First Reconsideration Order* also relaxed the local ownership limit, which had been one AM and one FM station per area, to permit common ownership of up to two AM and two FM stations, depending on the size of the market. Specifically, in markets with 15 or more stations, an individual or group may acquire up to two AM and two FM stations provided that the combined audience shares of those stations does not exceed 25 percent of the local radio market. In markets with fewer than 15 stations, a single owner may acquire a total of three stations, no more than two of which may be in the same service (*i.e.,* AM/AM/FM or AM/FM/FM), provided that the group owner's stations represent less than half of the total number of stations in the market. (The implementation of this rule is explained further below.) Finally, in the *First Reconsideration Order* the Commission declined to revisit its prior determination that certain time brokerage arrangements would be treated as attributable ownership interests for purposes of the multiple ownership rules.

3. Petitions for reconsideration of the *First Reconsideration Order* were filed by the League of United Latin American Citizens (LULAC), the National Association of Black Owned Broadcasters, Inc. and the National Black Media Coalition (NABOB/NBMC), and the Telecommunications Research and Action Center and the Washington Area Citizens Coalition Interested in Viewers' Constitutional Rights (TRAC/WACC). LULAC questions the propriety of the general rule relaxation, arguing that we should permit a licensee to increase the number of stations it owns in a market only where necessary to save a station from going off the air. LULAC and NABOB/NBMC challenge the revision of the minority ownership incentives in the national ownership rule and the establishment of a small business incentive. TRAC/WACC challenge the sufficiency of the rules governing time brokerage arrangements, contending that Commission staff determinations have not adequately held licensees accountable for brokered stations. The National Association of Broadcasters (NAB) filed comments with respect to all three petitions. Larry A. Duke, President of Duke Radio Broadcasting, Inc. and Duke Broadcasting Corporation (Duke), filed comments in the form of a letter concerning the definition of small markets for the purpose of applying the new ownership rules.

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[1] The *First Reconsideration Order* modified the Commission's initial decisions in this proceeding, adopted in the *Report and Order* in MM Docket No. 91-140, 7 FCC Rcd 2755 (1992) (*Report and Order),* before the rules adopted in the *Report and Order* became effective.

[2] Pursuant to the *First Reconsideration Order,* the national limit increased to 20 AM and 20 FM stations on September 16, 1994 (*i.e.,* two years after the effective date of the initial rules). 7 FCC Rcd at 6390. The Commission's initial determination in the *Report and Order* would have raised the national ownership limit to 30 AM and 30 FM stations. 7 FCC Rcd at 2765.

4. In addition, due to its relevance to the issues under evaluation in this proceeding, we herein consider, on our own motion, a Petition for Rule Making (RM-8414) filed by NAB concerning changes to the local radio multiple ownership rules as applied to small markets, and comments filed in response to that petition.[3] We also take this opportunity to provide greater specificity regarding the administration of certain aspects of the revised ownership rules. These clarifications are based on questions raised by radio licensees and other interested parties over the past two years.

5. Although we generally affirm the rules as adopted in the *First Reconsideration Order*, we are revising the national limits to increase the national cap for minority owners to 25 AM and 25 FM stations, and to raise to five the number, in excess of the national limits, of minority or small business-controlled AM or FM stations in which a non-minority broadcaster may hold a non-controlling interest. In addition, because of concerns raised by a number of parties with respect to the effects of the revised rules on competition and diversity in radio markets, on our own motion, we have reviewed the rules in light of relevant economic and antitrust principles. As set forth below, our analysis of these principles leads us to conclude that the rules, as adopted, are consistent with established principles of competitive analysis and at the present time provide adequate safeguards to ensure acceptable levels of diversity in the radio marketplace.[4]

II. ANALYTICAL FRAMEWORK

6. The Commission has a mandate to regulate radio broadcast licensees in the public interest.[5] In terms of the radio license ownership limits, there are two principal components of the Commission's "public interest" mandate – competition and diversity.[6] The Supreme Court has recognized that "the Commission has long acted on the theory that diversification of mass media ownership serves the public interest by promoting diversity of program and service viewpoints, as well as by preventing undue concentration of economic power."[7]

A. Diversity Issues

7. A primary foundation of ownership limits has been the concept of diversity of ownership. It has been the cornerstone of past analyses that diversity of owners (outlet diversity) leads to diversity of viewpoint (content diversity).[8] As the *Report and Order* in this proceeding notes, both outlet and content diversity have increased markedly in the past ten years. This resulted from not only a substantial increase in the number of radio stations but also from the development of new communications and mass media outlets.[9]

B. Competitive Issues

8. The public interest standard includes examination of competitive issues – indeed, the Commission is empowered to "make findings related to the pertinent antitrust policies, draw conclusions from the findings, and weigh these conclusions along with other important public interest considerations."[10] Competition is a means to the ends of maximizing consumer welfare and efficient allocation of resources. There appear to be other competitive substitutes for radio from the listeners' perspective – for example, music and talk format programs on broadcast and cable television, compact discs and music videos. There also may be reasonable substitutes for radio advertising from the advertisers' perspective, such as such as newspapers and billboards.[11] Given this increasing proliferation of competitors to broadcast radio, the Commission believes that the public interest is best served by greater reliance on competitive forces, rather than governmental regulation, to achieve these outcomes.

9. The competition aspect of the public interest primarily relates to protecting consumers and companies possibly subject to bottleneck monopolies due to the potential abuse of market power by a firm or a group of firms. The purpose of a competitive analysis is to determine whether in fact a firm or group of firms have and exercise such market power. Horizontal market share or concentration and barriers to entry are key factors in determining whether market power exists.[12] Regulatory barriers to entry in the radio market are significant – *e.g.*, applicants must obtain a license, such licenses are scarce, and assignments or transfers of licenses must be approved by the Commission. Thus, market share and concentration ratios may be more important in evaluating market power in radio markets than in many other markets.[13]

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[3] The NAB Petition was listed on an FCC *Public Notice*, Report No. 1996, released January 11, 1994. Only one party -- Duke -- filed responsive comments.

[4] Concurrently with this item, we are releasing a staff report analyzing the state of the radio industry in light of the 1992 relaxation of the ownership rules. *Radio Station Ownership Report*, FCC Mass Media Bureau, October 20, 1994.

[5] *See* Section 303 of the Communications Act, 47 U.S.C. § 303.

[6] *See Report and Order* at 2761.

[7] *FCC v. National Citizens Committee for Broadcasting*, 436 U.S. 775, 780 (1978).

[8] *See, e.g., Metro Broadcasting v. FCC*, 497 U.S. 547 (1990) (recognizes evidence demonstrating nexus between increased minority ownership and diversity of programming).

[9] *Report and Order* at 2757-58.

[10] *United States v. FCC*, 652 F.2d 72, 81-82 (D.C. Cir. 1980) (*en banc*) (quoting *Northern Natural Gas Co. v. FPC*, 399 F.2d 953, 961 (D.C. Cir. 1968)); *see also FCC v. RCA Comm., Inc.*, 346 U.S. 86, 94 (1952).

[11] For a recent analysis of own-price and cross-price elasticities of demand for advertising media, see Barry J. Seldon & Chulho Jung, *Derived Demand for Advertising Messages and Substitutability Among the Media*, 33 Quarterly Review of Economics and Finance 71-86 (Spring 1993). *See also* John C. Busterna, *The Cross Elasticity of Demand for National Newspaper Advertising*, Journalism Quarterly 347-351 (Autumn 1987).

[12] *United States v. Grinnell Corp.*, 384 U.S. 563, 571 (1966) (high market share may raise an inference of monopoly power).

[13] *See Oahu Gas Serv., Inc. v. Pacific Resources, Inc.*, 838 F.2d 360, 366 (9th Cir.) ("A high market share, though it may ordinarily raise an inference of monopoly power, will not do so in a market with low entry barriers or other evidence of a defendant's inability to control prices or exclude competitors."),

10. Market shares and concentration can only be assessed after relevant markets are determined. As a result, the first step in a competitive analysis is to define the relevant product and geographic markets. The Supreme Court has stated that in defining a product for antitrust law purposes, "no more definite rule can be declared than that commodities *reasonably interchangeable by consumers for the same purposes*" constitute one product market.[14] In general, the relevant geographic market refers to the area where buyers of the particular product can practicably turn for alternative sources of supply, or the area in which sellers sell this product.[15] No single geographic market definition is likely to be decisive for all purposes of examining a particular industry.[16] Assessment of potential market power is then made by identifying the buyers and sellers in these markets.

C. Application of Framework to Radio Broadcasting

1. Product and Geographic Market Definitions

11. The current radio ownership rules focus on the number of stations owned in national and local markets. The national limits view group ownership of radio stations located in New York City, Los Angeles and Pittsburgh as posing the same problem as group ownership of stations in Altoona, Pennsylvania, Paducah, Kentucky, and Effingham, Illinois.[17] The local limits are applied to New York City, where there are 43 commercial stations, in the same way they are applied to Lynchburg, Virginia, where there are 17 stations.

12. Radio stations operate in two distinct, yet related, markets, and the ownership restrictions impact both. Radio stations purchase or produce programming in a *radio programming production market*. Activity in the radio programming market can range from hiring a local disc jockey to picking up a satellite feed of the Super Bowl broadcast. Many programs, such as syndicated talk shows, "top-forty" shows, and sports programming can be obtained from national suppliers. Because radio stations can reasonably turn to other sources of supply outside of their local service area for much of their programming, we view the market for radio programming production as national in scope.[18]

13. Radio stations then distribute this programming in a complex local market and essentially derive their revenue by competing for listeners and advertisers. While listeners are able to receive the radio signal free of charge, listeners in essence "pay" for the service by listening to the advertising. As a result, the "buyers" in the *radio programming distribution market* are advertisers and listeners, and the "sellers" are radio stations. Because radio stations have limited signal contours, the radio programming distribution market is essentially local in character.

2. Impact of National Ownership Rules on Radio Programming Production Market

14. Since the *radio programming production market* operates on a national level as well as a local level, the extent of nationwide ownership of radio stations and the rules regulating such ownership could possibly impact this market. The Commission's radio station ownership rules address horizontal concentration of radio stations at the national level. Nationally, there is a total of 11,710 radio stations, 9,995 of them commercial."[19] The current rule allows that, under certain circumstances, one person may hold an attributable interest in up to 46 commercial radio stations nationally.[20] Forty-six stations out of 9,995 commercial stations do not even constitute one-half of one percent. Because of these low limits, a common measure of market power, the Herfindahl-Hirschman Index, would be extremely low (no more than 50), suggesting that current national ownership levels should not pose competitive problems in the programming production market.[21] In essence, the current rules require that there be at least 200 participants in the radio broadcasting industry nationwide. Indeed, while the current rule clearly prevents anticompetitive levels of concentration, it may also prevent efficiencies from joint ownership.

15. Diversity is the primary rationale for national ownership limits. As stated above, while the longstanding position of the Commission has been that diversity of owners

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cert. denied, 488 U.S. 870 (1988) (citations omitted); *see also United States v. Syufy Enterprises*, 903 F.2d 659, 664 (9th Cir. 1990)."

[14] *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 394 (1956) (hereinafter "*Cellophane*"); *see also Brown Shoe Co. v. United States*, 370 U.S. 294, 324-25 (1962). Cross-elasticity tests are used to determine close substitutes and measure the responsiveness of buyers and sellers of one product to a change in the price of a similar product. *See* Landes & Posner, *Market Power in Antitrust Cases*, 94 Harv. L. Rev. 937, 945-48 (1981); *see also* Network Inquiry Special Staff, FCC, New Television Networks: Entry, Jurisdiction, Ownership and Regulation 334 (1980) (hereinafter "Network Inquiry") ("[t]he relevant product market includes all products reasonably substitutable for each other at prevailing prices.").

[15] *Grinnell Corp.*, 384 U.S. at 575-76; *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320, 330-33 (1961); *Satellite Television & Associated Resources, Inc. v. Continental Cablevision of Virginia, Inc.*, 714 F.2d 351, 355 (4th Cir. 1983).

[16] *See, e.g.*, Network Inquiry, *supra* note 14, at 337-38 (in analyzing television, while "markets for television equipment and programs may reasonably encompass the entire nation, the geographic market for home viewed television programming might be extremely local").

[17] *See* Network Inquiry, *supra* note 14, at 362.

[18] *Grinnell*, 384 U.S. at 575-76.

[19] FCC Press Release, "Broadcast Station Totals as of September 30, 1994," Mimeo No. 50164 (released October 12, 1994).

[20] This figure of 46 total stations accounts for the current general limit of 20 AM and 20 FM stations, as well as the incentive permitting a non-controlling interest in an additional three stations per service that are controlled by minorities or small businesses. As detailed later in this item, we are increasing the minority ownership limit to 25 AM and 25 FM stations and we are raising the minority/small business incentive to five stations per service.

[21] The Herfindahl-Hirschman Index ("HHI") is a measure of industry concentration and is the sum of the square of the market shares of all industry participants. *See* F. M. Scherer and D. Ross, Industrial Market Structure and Economic Performance 72 (1990). According to the Department of Justice/Federal Trade Commission Merger Guidelines, industries with HHIs less than 1,000 are "unconcentrated" and mergers "are unlikely to have adverse competitive effects and ordinarily require no further analysis." *U.S. Department of Justice and Federal Trade Commission Merger Guidelines*, § 1.51(a), 57 Fed. Reg. 44,552 (1992) ("*Merger Guidelines*").

leads to diversity of viewpoint, the Commission in recent years has favored relaxing the national limits. When the Commission first revised the national ownership rules in 1984, it highlighted the tremendous growth in the number of media outlets since the rules were first adopted.[22] That growth and the large number of stations available ensure that the Commission's current, more flexible, rules do not inhibit diversity of viewpoint.

3. Impact of Local Ownership Rules on Radio Programming Distribution Markets

16. The issues regarding local concentration of radio station ownership are more complicated. Radio stations generate profits in the *radio programming distribution market* with advertising revenues greater than xthe total cost of production. A radio station having market power in a particular locality may exercisethis power either through increasing the price of advertising, lowering costs (perhaps lowering programming quality), or through a combination of the two. As a result, in small local markets, the presence of only a few rival radio station owners may raise competitive concerns that such markets could become highly concentrated.

17. In markets with fewer than 15 stations, the current rule allows one individual or entity to own up to three stations (no more than two of which may be in the same service), or fewer than half the total number of stations in the area, whichever is less. As a result, a market with five to nine stations might have only three separate owners, depending on the distribution of AM and FM stations. As a result, a nine-station market could end up being regarded as "highly concentrated" under the DOJ/FTC merger guidelines.[23] These five- to nine-station markets represent a very small segment of the radio industry, however, given that approximately 75 percent of the U.S. population lives in markets with 15 or more radio stations.

18. In local markets with 15 or more radio stations, the current rule prevents ownership beyond four stations (two AM and two FM) and imposes a combined audience share cap of 25%. The current rules therefore permit, in markets with 16 stations, for example, as few as four groups of four stations, which would still be considered "highly concentrated" under the merger guidelines. In larger markets, however, the rules tend to create an "unconcentrated" structure, since even in the largest local markets no entity may own more than four stations. For example, in New York City, where there are 43 commercial stations, no one person may own more than 9.3% of these radio stations.[24]

19. The 1992 increase in the local ownership limits was based on the Commission's belief that consolidation of ownership can provide significant benefits to the radio industry. As discussed previously in this docket, common ownership of radio stations in a single local market permits those stations to function cooperatively with respect to advertising sales, programming, promotion, production and other operations. Group ownership also allows for the sharing of studio space, equipment and other resources.[25] By lowering overall operating costs, such consolidation may permit a station to spend more money on programming quality and to lower advertising rates. In turn, consolidation may enable group-owned stations to become more vigorous competitors in the marketplace than they would be individually.

20. The local ownership rules are also based on diversity grounds. As pointed out above, outlet diversity at the local level has risen in recent years. The past ten years have seen not only a substantial increase in the number of radio stations,[26] but also an increase in other competing media outlets. The Commission pointed out this substantial increase in the number and variety of competing mass media providers in relaxing the contour overlap definitions germane to the local radio ownership rule in 1989.[27]

21. In addition, higher levels of concentration may actually increase diversity, especially in small markets. For instance, the 1970 Commission decision allowing AM-FM combinations in the same local area was predicated on the observation that unless AM-FM combinations were allowed, the FM allocations might remain unused.[28] Thus, a small market may be better served by permitting three licensees to own six radio stations (*i.e.*, two stations each), rather than by permitting three licensees to own three radio stations (*i.e.*, one station each) and letting the other three stations remain off the air. In addition, multiple ownership may well encourage program content diversity because a firm owning several competing local stations has a strong incentive to program those stations with different formats in order to compete for different segments of the audience. Separate owners, on the other hand, might be more likely to direct their programming at the same listeners and follow similar formats.[29]

22. In sum, a competitive analysis of the local ownership rules suggests possible problems with the current ownership restrictions in small markets where few stations exist and substantial market concentration is permitted. On the other hand, there is not enough data in this record to draw any conclusions concerning whether these levels of concentration hinder or may actually help achieve optimum

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[22] *See Report and Order* in Gen. Docket No. 83-1009, 100 F.C.C. 2d 17 (1984), *reconsidered*, 100 F.C.C. 2d 17 (1985). That proceeding raised the overall national ownership limits for radio and television from seven stations per service to 12 stations per service. It did not encompass the local ownership rules.

[23] *See Merger Guidelines*, *supra* note 21, at § 1.51(c).

[24] The 43-station total is based on Arbitron data for the market and therefore includes only those stations that meet Arbitron's minimum reporting standards. *See Report and Order*, 7 FCC Rcd at 2778 n.100. As a result, the actual number of stations received by listeners in the market may be significantly greater.

[25] *Report and Order* at 2760-61; *First Reconsideration Order* at 6388.

[26] The number of FM radio stations has grown from 4,374 in 1980 to 6,762 today, an increase of 55 percent. The number of AM stations has risen from 4,589 in 1980 to 4,925 today (7 percent).

[27] *See First Report and Order* in MM Docket No. 87-7, 4 FCC Rcd 1723 (1989). That proceeding retained the one AM/one FM limit but permitted a single owner to acquire stations in closer proximity than was previously allowed by revising the relevant overlapping signal contours from 1 mV/m to 5 mV/m for AM and from 1 mV/m to 3.16 mV/m for FM.

[28] The Commission noted that allowing common ownership "will preclude the possible demise of many FM stations." *First Report and Order* in Docket No. 18110, 22 F.C.C.2d 306, 319 (1970), *reconsidered*, 28 F.C.C.2d 670 (1971).

[29] *See* Steiner, *Program Patterns and Preferences, and the (Workability of Competition in Radio Broadcasting*, 66 Q. J. Econ. 194 (1952).

market performance. Finally, as noted in the staff's *Radio Station Ownership Report,* released concurrently with this item, there has been too little experience under the new rules to make any conclusions regarding the impact of our relaxed local radio ownership restrictions.

23. Given this analytical framework, we now turn to the specific issues raised by the petitioners for reconsideration of the *First Reconsideration Order.* First, we take up petitioners' requests that we revise the local ownership rules. We next consider petitioners' requests that we modify the national minority ownership caps. Finally, we will consider other issues raised by petitioners, including the treatment of time brokered stations and specific questions regarding implementation of the ownership rules.

III. LOCAL OWNERSHIP LIMITS

24. The *First Reconsideration Order* revised Section 73.3555 to permit a single owner in a larger market to own up to two AM and two FM stations, subject to an audience share cap of 25 percent, and to permit an owner in a smaller market to own up to three stations, provided that no more than two are in the same service and that the stations represent fewer than half of the total number of stations in the area.[30] A "market" is defined with respect to overlapping signal contours. For instance, the relevant market with respect to a combination of two stations in the same market would encompass those two stations as well as all other radio stations whose principal community contours overlap those of the two stations involved in the proposed transaction.

A. LULAC and NABOB/NBMC

25. LULAC argues that the new local rules disadvantage small stations. It contends that while large and profitable stations gain market power through consolidation, small stations will see their market shares decrease and will be unable to find financing for their own consolidations. In this regard, NABOB/NBMC reiterate their previous argument that increased ownership limits will substantially reduce opportunities for increased minority ownership in broadcasting and will force minority broadcasters out of the radio industry.[31] LULAC restates the suggestion it raised in its previous petition for reconsideration that, rather than change the local ownership rules, the Commission should "expand the 'failed station' doctrine" to permit common ownership of radio stations "that need economies of scale in order to remain economically viable."[32] LULAC also takes issue with the Commission's characterization in the *First Reconsideration Order* of its proposal as one that would virtually require a station to leave the air before receiving assistance. In this regard, LULAC notes that a station could be considered failed or failing if, for example, it could "show its likely decline, through financial projections prepared by an outside expert."[33] LULAC asserts that allowing mergers between failing stations will provide the benefits of common ownership to those stations that need them, while retaining the more restrictive local ownership rule, and the diversity benefits achieved by the prior rule, for all other stations.[34]

26. In opposition, NAB contends that adoption of LULAC's proposed failed station standard, in lieu of the ownership limitations adopted in the *First Reconsideration Order,* would impede the positive effects of the new rules. NAB submits that the new rules, by affording relief to all stations, will benefit consumers generally by not only allowing struggling radio stations to remain operational, but by also increasing competition throughout the radio industry by increasing its overall economic strength.[35]

27. *Discussion.* The Commission directly addressed LULAC's suggestion to adopt a failed station standard in the *First Reconsideration Order.* The Commission stated:

> This "failed station" standard is insufficient to achieve the goals of this proceeding because it would focus on the health of a few individual stations rather than the vitality of the industry as a whole. Moreover, under such a standard, stations would virtually have to leave the air before they could receive assistance. We prefer a rule that would assist stations before they reach the point of failure.[36]

LULAC's argument, that its "failing" station standard would permit a troubled station to obtain ownership relief well before it actually fails, does not adequately address our fundamental concern with the vitality of the industry generally. We remain persuaded that the benefits, to both radio stations and consumers, from increased ownership efficiencies should not be limited to failing or failed stations. LULAC has presented no new evidence or argument, and we find no independent basis to revisit that view. NABOB/NBMC likewise have not presented any new information that would persuade us to further modify the local limits; we will address their overall concerns regarding the national limits in Section IV, *infra.* In sum, consistent with our analysis of competition and diversity issues germane to the industry, and consistent with our evaluation of the benefits of increased group ownership identified previously in this proceeding,[37] we continue to believe that the rules as adopted are necessary to invigorate intra-industry competition and include adequate safeguards to ensure that diversity of viewpoint is maintained.

28. While we decline to modify our local ownership rules, we take this opportunity to make a minor correction. A reference to "the most recent published audience share data available at the time that the application is filed" was deleted from Section 73.3555(a)(3)(iii) when that rule section was revised (and renumbered) pursuant to the *First Reconsideration Order.* That deletion was inadvertent, and the quoted provision was intended by the Commission to remain in the rules.[38] Section 73.3555(a)(3)(iii) will be modified to reinsert that language, as set forth in the Appendix.

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30 *First Reconsideration Order,* 7 FCC Rcd at 6393-94.
31 NABOB/NBMC Petition at 3, 9-10.
32 LULAC Petition at 4.
33 *Id.* at 5.
34 *Id.* at 3-5.
35 NAB Comments at 4-6.
36 *First Reconsideration Order,* 7 FCC Rcd at 6390 n.19.
37 *See Report and Order* at 2773-76; *First Reconsideration Order* at 6388, 6393.
38 *Franklin Communications Partners, L.P.,* 8 FCC Rcd 4909, 4911 (1993).

B. NAB and Duke

29. In its petition for rule making, NAB maintains that while the revised ownership rules will provide benefits to most radio broadcasters, there are instances, particularly in smaller markets, where strict application of the market definitions in the rules could yield results opposite those intended by the Commission. Specifically, NAB points to cases where a station with a large signal contour is licensed to a small community and seeks to combine or enter into a time brokerage arrangement[39] with another station licensed to the same area. While the stations only truly compete in the small market, NAB contends, the proposed combination may nonetheless be evaluated under the large market rules, including the 25 percent audience share cap, because the wide contour of one of the stations can result in more than 14 stations being considered part of the relevant market. This anomalous result, NAB argues, would leave the stations "without access to the benefits of consolidation and cost efficiency."[40] Thus, while NAB generally commends the principal community contour-based market definitions adopted in this proceeding, it contends that some adjustment in this approach is needed in cases such as it has described.

30. NAB accordingly suggests that when only one of the stations in a proposed combination has a principal community contour that would place the transaction in a market of 15 or more stations, the parties to the transaction should be permitted to elect how the transaction will be evaluated. NAB suggests that such licensees choose to be governed by either (1) the rules for small markets based on the number of stations overlapping the smaller facility's contour (thus avoiding the audience share limitation); or (2) the rules for large markets, but with the audience share calculated based on all counties receiving any one of the 15 or more stations counted as in the market pursuant to Section 73.3555(a)(3)(ii).[41]

31. Duke raises similar concerns with the contour-based market definitions in the new rules when applied in "small" markets, but proposes a very different solution than that offered by NAB.[42] To resolve this situation, Duke suggests a delineation of two tiers of markets based on Metropolitan Statistical Area (MSA) ranking, with "larger" markets still subject to the combined audience share limitation of 25 percent, and "smaller" markets not subject to the combined audience share limitation in the absence of a showing that the particular combined share exceeding 25 percent creates an excessively high concentration of audience. He specifically proposes that MSAs ranked above 150[43] would be placed in the "larger" market tier, while those MSAs ranked 150 and below, as well as non-MSA markets such as Jonesboro, would be placed in the "smaller" market tier.[44]

32. Turning to another aspect of the smaller market rules, NAB asserts that because broadcasters in markets with fewer than 15 stations are now limited to less than half, rather than up to half, of the market's stations, a station owner in a market with four or fewer stations cannot acquire even a failing station in need of "rescue," and the owner of a preexisting AM/FM combination cannot acquire another station in the market unless there are at least seven stations in the market. Therefore, NAB suggests that the local ownership rule be modified so that ownership of "not greater than 50 percent" of the stations in a market would be permitted rather than the current "less than 50 percent" rule. This would allow, NAB argues, the rescue of failing or dark stations by a successful broadcaster in a genuinely small market. In addition, NAB contends that any single station or AM/FM combination licensee should be allowed in all situations to add one additional station to common ownership.[45]

33. In suggesting its refinements, NAB believes that small market broadcasters would be able to take advantage of the benefits and efficiencies of the new ownership and time brokerage rules articulated in the *First Reconsideration Order* without significantly changing the concentration of control in local radio and advertising markets. In this regard, NAB states that the additional consolidation of small market radio stations that could result, however modest, outweighs any possible or perceived detriments. In fact, NAB suggests that small markets may become even more competitive if certain local radio stations realize efficiencies from consolidation and become stronger competi-

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[39] For a detailed discussion of issues regarding time brokerage, see Section V, *infra*.

[40] NAB Petition at 3.

[41] *Id.* at 14. NAB points to the case of certain stations in Bismarck, North Dakota, as exemplifying the "anomalous" small market problem it has raised. We note that the licensees of the stations involved in that example separately filed a request for declaratory ruling seeking relief from the audience share limitations of the rules. Because the request raises factual arguments specific to the circumstances in that case, we will address the merits of the declaratory ruling request separately.

[42] As an example of the small market problem, Duke describes his own attempts to acquire KBTM(AM) and KJBR-FM, Jonesboro, Arkansas, while retaining control of an FM station, KFIN, also licensed to Jonesboro. Duke relates that Jonesboro, a community of just over 45,000, is neither a Metropolitan Statistical Area nor an Arbitron market, and is ranked as the 176th television market. These factors, in Duke's estimation, suggest that his attempt to acquire another broadcast facility in Jonesboro be evaluated as one involving a "smaller" market. However, Duke asserts that by virtue of the signal contour of KJBR-FM, a Class C station, the area encompassed by the combined contours of the stations he proposed to own was overlapped by the principal community contours of 38 other stations, including five from Memphis, Tennessee, over 60 miles from Jonesboro, making his proposed acquisition subject to the evaluation accorded "larger" (15 or more stations) markets. In these circumstances, Duke contends that the overlapping contour approach distorts the market by encompassing areas "well beyond the ability to influence the market where the proposed merger is located." *Letter to Chairman Sikes*, dated October 12, 1992, at 1. He believes that the Commission did not intend for a market like Jonesboro to be placed in the same category as larger markets like Memphis and Little Rock as a result of such signal overlap. In *Patteson Brothers, Inc.*, 8 FCC Rcd 7595 (1993), the Commission refused to grant Duke a permanent waiver of the rules, concluding that an insufficient showing had been made to overcome the *prima facie* concern raised by the rule that the combination could lead to excessive concentration.

[43] The 150th MSA is Appleton-Oshkosh-Neenah, Wisconsin, which has 13 stations licensed within the MSA.

[44] In this regard, Duke states that there are 350 cities with a population of 50,000 that qualify as MSAs in the United States, and he asserts that the smallest MSA with more than 15 radio stations is the 258th-ranked Lynchburg, Virginia, MSA with 17 stations. *Letter to Chairman Sikes*, dated October 12, 1992, at 2.

[45] NAB Petition at 15-16.

tors offering increased program diversity. In addition to the benefits to be realized by smaller market broadcasters, NAB maintains that the public is appropriately served by stations with greater financial health and potential to provide service, particularly where the alternative would be dark or failing stations.[46]

34. Finally, in the event the above changes are not adopted, NAB believes that a clear and liberal set of criteria should be established for requests for waiver of the local ownership rule in traditionally small markets. Among the critical elements of any waiver policy, according to NAB, would be the effort to save a dark or failing station.[47]

35. *Discussion.* We are not persuaded by NAB or Duke to forego the present scheme of overlapping signal contours to determine the number of stations in a market for evaluating proposed common ownership, or otherwise to modify the application of the rules. In designing the signal overlap standard, the Commission opted for a realistic measure of the potential impact of proposed common ownership on competition and diversity, and specifically rejected suggestions that Arbitron data, MSAs (proposed by Duke here) or other narrow geographic designations be employed to count the number of stations in a market. The Commission stated:

> We believe that the use of this station [contour overlap] counting method will address our core concerns of competition and diversity. We are convinced by petitioners' arguments that this revised measure will reflect the actual options available to listeners and will reflect market conditions facing the particular stations in question.[48]

There is no evidence to suggest that the rationale underlying the adoption of the contour overlap approach -- a more accurate measure of where a station's signal can be adequately received and, therefore, where it can compete for listeners -- is any less appropriate for stations in smaller markets under the circumstances presented by NAB and Duke. A station combination with an aggregate principal community contour overlapped by 15 or more stations can be expected to compete for listeners with those stations, and the audience share cap is applied in such a case as an additional safeguard intended to identify potential concentration problems that may threaten diversity and competition.[49] Moreover, the Commission has recognized that the signal overlap standard is likely to be conservative in counting the stations receivable by listeners because, in some instances, listeners may be able to receive signals beyond the predicted principal community contour of a particular station.[50]

36. We decline to, in effect, ignore those stations, such as Class C FM stations, with superior signal coverage. We also decline to redefine the area to which county-by-county audience share calculations apply in the manner suggested by NAB. We believe the suggested change would unduly dilute the diversity and competition safeguards adopted in our previous orders, and, in any event, would not reflect competitive conditions in the areas in which stations proposed to be combined provide the majority of their service, *i.e.*, within their principal community contours.

37. With respect to NAB's other proposals, the Commission has already expressly rejected a change of the rule applicable to markets of fewer than 15 stations to permit ownership of "*up to* 50 percent of the stations in [such] a market . . . rather than the adopted limit of *less than* 50 percent, [because it] could result in an unwarranted level of consolidation in too many markets." *First Reconsideration Order,* 7 FCC Rcd at 6394 (emphasis in original).[51] On the record before us, and consistent with our above analysis of competition and diversity in the radio industry, we continue to believe that NAB's suggestions to permit "not greater than 50 percent" ownership in a given radio market, or, for that matter, an across-the-board increase of one station per single station or AM/FM combination licensee, "presents too great a potential to dominate the local radio market." *Id.* Further, we are not persuaded that the 3specific changes NAB advocates are warranted as a means of rescuing failing or dark stations. First, as proposed, these changes would be applicable without regard to the circumstances of an individual facility or its financial condition, and would have the potential to increase concentration significantly. Second, cases involving a genuine threat of station failure can be and are best considered by a waiver process that can appropriately account for the specific factual circumstances at hand.

38. Moreover, we are not persuaded that a specific set of criteria need be established to govern "small market" waiver requests generally. Because of the variety of particular circumstances that may be present in any given radio market, we believe that any requests for waiver of this particular rule should not be limited at this point to specific criteria.[52] Rather, we believe that any deviation from our local ownership rule must be based on a specific showing that the facts of a particular case warrant an exception and that the requested action is consistent with the overall objectives of that rule in the individual market under examination. The facts adduced in support of a waiver may, in any given case, include evidence that one station is facing particular financial difficulties; however, we shall not require such a showing as a precondition to every waiver request, nor shall such a showing necessarily be sufficient to justify grant of a waiver.

C. Summary

39. In sum, applying the principles of competition and diversity discussed earlier in this document, we are not persuaded by petitioners to further modify our restrictions on local multiple ownership to make them either more restrictive or more lenient at this time. The petitioners' arguments that the revised local rules will prejudice small station owners and minority broadcasters, as well as the

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[46] *Id.* at 9, 13-16.
[47] *Id.* at 16-17.
[48] *First Reconsideration Order,* 7 FCC Rcd at 6395.
[49] *See First Reconsideration Order,* 7 FCC Rcd at 6396; *Report and Order,* 7 FCC Rcd at 2779.
[50] *Report and Order,* 7 FCC Rcd at 2779.
[51] The effect of the "less than 50 percent" provision is to limit common ownership to either two stations (markets with 5 or 6 stations) or to preclude common ownership altogether (markets with 4 or fewer stations), unless the combination is AM/FM, which is expressly permitted in all circumstances.
[52] *See, e.g., WAIT Radio v. FCC,* 418 F.2d 1153 (D.C. Cir. 1969).

contrary arguments that the rules are unduly restrictive, were all fully addressed in the *First Reconsideration Order,* and no party has raised a compelling new argument on this point. The Commission has already stated its belief that small market or struggling stations can benefit from the relaxed local rules in that the new rules permit them to consolidate resources with other stations. We also recognize, as mentioned in Section II, *supra,* that increased consolidation may potentially lead to undue market concentration and decreased diversity of viewpoint in certain very small markets. Nonetheless, we continue to believe that concerns about the impact of the rule changes on some small stations that might face stiffer competition are "outweighed by the considerable public benefit we anticipate from a general strengthening of stations as a result of an increase in the local ownership limits."[53] In any event, as noted in the staff's *Radio Station Ownership Report* released concurrently with this item, there has been too little experience under the new rules to conclude that our predictions in relaxing the local ownership restrictions were ill-founded. We intend to continue to monitor the effects of the relaxed rules and will take further action as necessary.

IV. MINORITY OWNERSHIP AND SMALL BUSINESS INCENTIVES

40. The Commission, in 1985, relaxed its national broadcast ownership limits to permit any single individual or entity to control up to 12 stations in each broadcast service (AM, FM and TV).[54] It also determined that a minority incentive should be included in the new rules and therefore permitted "group owners of television and radio stations . . . to utilize a maximum numerical cap of 14 stations provided that at least two of the stations in which they hold cognizable interests are minority controlled."[55] Under this provision, non-minority multiple owners could control 12 stations and hold a non-controlling but cognizable interest in two additional stations. Minority-controlled multiple owners could directly own and control the additional two stations.

41. The *Report and Order* in this proceeding declined to incorporate minority incentives in the revised national multiple ownership rules that it adopted. The *First Reconsideration Order,* however, reinstated and expanded one aspect of the former rule's minority incentive provision by permitting all multiple owners to hold a cognizable, but non-controlling, interest in an additional three AM and three FM stations that were minority-controlled. Unlike the prior rule, the revised rule did not permit minority multiple owners to hold a controlling interest in the additional stations. The new rule also expanded the class of entities that could control the additional stations to include not just minorities, but small businesses as well.[56]

42. NABOB/NBMC urge the Commission to reinstate the aspect of the prior rule that permitted minority-owned companies to take a controlling interest in additional stations above the national ownership caps. They argue that in revising the rule, the Commission focussed on how to encourage investment in minority broadcasters, when the ultimate goal should be how to increase minority ownership. In other words, NABOB/NBMC contend that the fostering of investment by non-minority companies in minority-owned stations should not be of itself an "end," but rather a "means" to the end of increased minority ownership. NABOB/NBMC maintain that the change from the prior rule will have a negative impact on overall minority ownership because it will decrease the total number of stations that can be controlled by existing minority licensees, and, with the increase of the national ownership limits generally, will lead to further concentration of ownership in the broadcast industry, diluting substantially the opportunities for increased minority ownership of broadcast facilities.[57]

43. NABOB/NBMC also contend that the *First Reconsideration Order* did not provide evidence with which to evaluate the effect of the rule changes on minority ownership, and they reiterate their argument, rejected in the *First Reconsideration Order,* that the Commission's appropriations legislation prohibits modification of the minority ownership incentive.[58] Further, NABOB/NBMC reiterate their request, denied in the *First Reconsideration Order,* that the national ownership limits be returned to 12 stations per service, claiming that any increase would lead to further concentration of ownership in the broadcast industry and substantially reduce opportunities for increased minority ownership.[59]

44. LULAC, NABOB/NBMC and NAB urge the Commission to repeal the small business incentive established in the *First Reconsideration Order.* LULAC and NAB argue that adoption of the small business incentive violated the Administrative Procedure Act (APA), 5 U.S.C. §553, because such an incentive was not proposed in the initial *Notice of Proposed Rule Making* in this proceeding.[60] LULAC and NABOB/NBMC view the small business limitation as a "loophole in the national ownership limits" that is open to abuse.[61] For example, they contend, a group owner may set up a family member or business associate as a "small business," or a corporation could set up another corporation whose stock is held by its own stockholders.[62] Further, the petitioners maintain that the small business incentive will dilute or otherwise undermine the Commission's efforts to increase minority ownership in radio by vitiating any incentive for group owners to invest in minority-controlled stations.[63] NAB similarly suggests that be-

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[53] *First Reconsideration Order,* 7 FCC Rcd at 6393-94.

[54] *Memorandum Opinion and Order* in Docket 83-1009, 100 FCC 2d 74 (1985).

[55] *Id.* at 94.

[56] "Small business" was defined as an individual or entity with annual revenues of less than $500,000 and assets of less than $1,000,000, including all affiliated entities under common control. *First Reconsideration Order* at 6391. Because this definition was adopted prior to enactment of the Small Business Credit and Business Opportunity Enhancement Act of 1992, Pub. L. No. 102-366, 106 Stat. 999 (enacted September 4, 1992), prior approval of the Commission's use of this definition by the SBA was not required.

[57] NABOB/NBMC Petition at 5-10.

[58] *Id.* at 7-9.

[59] *Id.* at 3.

[60] LULAC Petition at 9-10; NAB Comments at 9.

[61] NABOB/NBMC Petition at 6.

[62] LULAC Petition at 7-8; NABOB/NBMC Petition at 6-7.

[63] LULAC Petition at 6-7, NABOB/NBMC Petition at 6-8, NAB Comments at 7-9.

cause the small business incentive could weaken minority ownership provisions, that initiative may be at odds with Congressional intent to promote minority ownership.[64]

45. *Discussion.* We continue to believe, as discussed both above and previously in this docket, that further expansion of the national ownership limits would not hinder diversity of viewpoint and could spur competition in the industry. The arguments raised by petitioners with respect to the increase in the general national ownership limits from 12 stations per service to 20 stations per service were fully addressed earlier in this proceeding. Because petitioners present no new arguments or evidence on this subject, we find no basis to revisit our earlier conclusions in raising the national ownership limits.

46. We are persuaded by petitioners, however, that permitting minority owners to hold a controlling interest in additional radio stations will serve the goal of increasing minority ownership without posing a significant threat to competition or diversity. We will therefore amend Section 73.3555 of our rules to permit minority owners to own and control additional stations over and above the general national caps. Moreover, based on our belief that further national consolidation is appropriate, we will increase from three to five the number of additional stations per service that may be acquired pursuant to the incentive. Our aim in making these modifications is to permit minorities to own more stations as well as to make the investment incentive aspect of the rule more attractive to large group owners.

47. We are not persuaded that we should delete the small business incentive. We believe that our current application processing standards, which involve a case-by-case analysis of each transaction, are sufficient to guard against sham small business applications. With respect to petitioners' arguments regarding notice, we point out that the *Notice of Proposed Rule Making* in this proceeding invited commenters to discuss a range of issues regarding the national ownership caps, and some commenters emphasized that access to capital is a problem for new entrants and small businesses in general, not just minority-owned entities.[65] As a result, the *First Reconsideration Order* concluded that adopting both minority and small business incentives would be appropriate. Further, we note that we intend to explore minority ownership issues in an upcoming proceeding, with an eye toward eliminating barriers currently facing minorities seeking to enter the industry or expand their present holdings. We plan to use that proceeding to consolidate outstanding proposals related to minority ownership as well as to gather and evaluate new ideas.[66] This approach will permit us to formulate a more comprehensive view of the problems facing minority broadcasters specifically, and to develop a regulatory framework that addresses those problems in as complete and as effective a manner possible.

48. In sum, minority owners will be permitted to own and control up to 25 AM and 25 FM stations. Non-minority owners will be permitted to own and control up to 20 AM and 20 FM stations per service and may hold a non-controlling interest in five additional stations per service, provided that those additional stations are controlled by minorities or small businesses. *See* Appendix.[67]

49. We note that, pursuant to the rules adopted in the *First Reconsideration Order,* our national ownership limits automatically increased from 18 AM and 18 FM to 20 AM and 20 FM on September 16, 1994. On October 7, 1994, NABOB and NBMC filed a "Joint Motion for Rescission and Stay" asking us to rescind the automatic increase and stay the effective date of that increase. Specifically, they request that the rules be held in abeyance until the Commission has acted on their petition for reconsideration and evaluated the effect of the 18 AM/18 FM cap on minority ownership. We resolve NABOB/NBMC's petition for reconsideration in this *Second Reconsideration Order.* Moreover, our *Radio Station Ownership Report* analyzes the effect that the increase in our national caps has had on minority broadcasters to the extent presently possible. Accordingly, we find the request for stay of our rules to be moot, and the request for rescission is denied.

V. TIME BROKERAGE ARRANGEMENTS

50. As we stated in the *Report and Order,* "time brokerage is a type of joint venture that generally involves the sale by a licensee of 'discrete blocks of time to a "broker" who then supplies the programming to fill that time and sells the commercial spot announcements to support it.'"[68] The *First Reconsideration Order* affirmed the Commission's holding in the *Report and Order* that if a time brokerage agreement between two stations in the same market involves more than 15 percent of the brokered station's programming per week, the brokered station will be treated as if it was owned by the brokering station for purposes of the national and local ownership rules.[69]

51. TRAC/WACC's petition for reconsideration of the *Report and Order* argued that various staff rulings in time brokerage cases were contrary to law and policy in that they permitted "excessive delegation of programming control in violation of the Communications Act." In the *First Reconsideration Order,* the Commission responded:

> TRAC improperly seeks reconsideration here of staff decisions issued two years ago. We believe that determinations regarding a licensee's retention of control of its time brokered station are most appropriately

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[64] NAB Comments at 7-9.

[65] *See First Reconsideration Order* at 6390.

[66] For example, the forthcoming minority ownership item will likely incorporate the "incubator" program approach presented in the *Further Notice of Proposed Rule Making* in this proceeding, 7 FCC Rcd 6387, 6391 (1992), and certain aspects of the *Notice of Proposed Rule Making and Notice of Inquiry* regarding sources of capital, 7 FCC Rcd 2654 (1992).

[67] While we have concluded that there are sound policy reasons to alter the revisions to the minority incentive provisions of the radio ownership rules adopted in the *Report and Order* and the *First Reconsideration Order,* we again reject petitioners' view that those revisions were contrary to the Commission's appropriations legislation. That legislation prohibits the Commission from altering its comparative licensing, distress sale and tax certificate policies relating to minorities, and nothing we have done in this proceeding has altered those policies. *See* Departments of Commerce, Justice and State, the Judiciary, and Related Agencies Appropriations Act, 1993, Pub. L. No. 103-121, 107 Stat. 1153 (1992).

[68] 7 FCC Rcd at 2784.

[69] First Reconsideration Order, 7 FCC Rcd at 6400-01.

made on a case-by-case basis. This has been and will continue to be our practice in the time brokerage area.[70]

52. In their instant petition, TRAC/WACC take exception to that response, suggesting that it did not reach the core of the issue presented – licensee compliance with the Communications Act and control of programming. TRAC/WACC reiterate that licensees must remain responsible for compliance with, among other things, equal employment opportunity policies, sponsorship identification, and format and programming choices, and again contend that the staff rulings are permitting improper delegation of these licensee responsibilities. In this regard, TRAC/WACC argue that the Commission should not be "bound in future rule makings by policy decisions of its staff made in *ex parte* informal adjudications."[71] TRAC/WACC also note that members of the public are not given notice of, and may not have standing to participate in, declaratory rulings at the staff level. As a result, the Commission's cited statement in the *First Reconsideration Order* is read by TRAC/WACC to suggest that the only way for issues of control to be explored is by the timely filing for reconsideration of staff letters approving of time brokerage agreements. TRAC/WACC contend that this approach would undermine full participation and informed decision making in this critical area. TRAC/WACC insist that the Commission must carefully address this issue to ensure that the fundamental principle of ultimate licensee responsibility is not abandoned.[72]

53. In opposition, NAB argues that the revised time brokerage rules and policies, as adopted and applied by the staff in its rulings, are lawful and are designed to adequately ensure that licensees do not relinquish control of their stations and remain responsive to the obligations of a licensee. It maintains that the rule requires broadcasters to comply with a reasoned set of limitations and to submit relevant information to the Commission and the station's public files. NAB therefore believes that these requirements satisfy all of the legitimate substantive and procedural concerns of TRAC/WACC.[73]

54. *Discussion.* The language of the *Further Reconsideration Order* cited by TRAC/WACC was not meant to imply that these time brokerage issues were somehow closed, but rather was intended to reflect our continuing view that particular situations are better resolved on a case-by-case basis. The specific aspects of time brokerage arrangements questioned by TRAC/WACC here were thoroughly discussed in the *Report and Order*. There the Commission stated its concern "that widespread and substantial time brokerage arrangements among stations serving the same market, in concert with the increased common ownership permitted by our revised local rules, could undermine our continuing interest in broadcast competition and diversity."[74] As a result, the Commission adopted restrictions on time brokerage arrangements so that they will be counted as ownership interests where significant brokering between competing stations is involved. Furthermore, we have clearly stated that control, including ultimate authority over programming decisions, must be retained and exercised by brokered stations,[75] and our staff rulings have consistently emphasized that ultimate control of a station must rest with the licensee.[76] TRAC/WACC has not introduced any new arguments to convince us that we need to take further action in this proceeding with respect to this, or other aspects, of time brokerage.[77] Moreover, we believe that imposition of any additional restrictions on these arrangements would run counter to one of our objectives in this proceeding, which was to strengthen the radio industry by giving radio broadcasters more flexibility. We will, however, continue to review allegations of transfers of control in specific cases. In this regard, we note that control issues relating to time brokerage agreements can arise in the renewal context and not simply in the context of requests for declaratory rulings.

55. In light of various questions informally presented to the staff and based on our experience since these time brokerage provisions were adopted, we do believe that it is appropriate to offer more specific guidance on the application of the rules to time brokerage agreements between stations in the same local market. The Commission previously decided not to require the termination of an agreement that does not comply with the local ownership rules if the agreement was entered into prior to the effective date of the rules.[78] These agreements are, in effect, "grandfathered." We have received informal inquiries concerning whether "grandfathered" time brokerage agreements in "larger" markets may be renewed if the combined audience share of the stations exceeds 25 percent at the time that the initial agreement expires. We have received similar inquiries concerning the permissibility of renewing time brokerage agreements entered into after the effective date of the rules if the combined audience share of the stations at the time of expiration/renewal exceeds 25 percent. Additionally, we have received inquiries concerning whether the contract rights associated with time brokerage agreements may be assigned when the brokering station is sold.

56. In the *Report and Order* and the *First Reconsideration Order,* the Commission did not specifically state whether time brokerage agreements may be renewed by the parties or transferred to third parties. We believe that a clear statement in this *Order* of our view on these matters would be helpful both to applicants and to the Commission.

57. When a brokering station is sold, an existing brokerage agreement that would be barred by the rules if entered initially at the time of the sale, may be transferred, subject to the limitation outlined in paragraph 58, *infra.*

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[70] *Id.* at 6401.
[71] TRAC/WACC Petition at 2-4.
[72] *Id.* at 4-5.
[73] NAB Comments at 6-7.
[74] *Report and Order,* 7 FCC Rcd at 2788.
[75] *See First Reconsideration Order,* 7 FCC Rcd at 6401-02.
[76] *See, e.g., Letter to Gisela Huberman,* 6 FCC Rcd 5397 (Mass Media Bureau 1991); *Letter to Roy R. Russo,* 5 FCC Rcd 7586 (Mass Media Bureau 1990).
[77] With respect to TRAC/WACC's concern that the public be permitted to participate in matters involving time brokerage determinations, we note that members of the public may, in the ordinary course, bring matters to the Commission's attention by filing a complaint or raising a challenge in the context of a pending renewal, transfer or assignment application. We do not believe, however, that our procedures must now be amended to permit formal public notice and comment on declaratory rulings in this context.
[78] *First Reconsideration Order,* 7 FCC Rcd at 6402.

The new owner may enjoy all rights and limitations with respect to our multiple ownership rules as the original owner, but only for the duration of the term of the agreement in effect at the time of transfer. Thus, if a licensee's combined audience share in a large market for a station it owns and one it brokers grows to exceed 25 percent during the term of the agreement (or if it exceeded 25 percent initially but was grandfathered), that licensee's interests can be sold as a combination and the brokerage agreement can continue in effect for the duration of the initial term of the brokerage agreement. Similarly, if a grandfathered brokerage agreement in a smaller market permitted a licensee to own and broker stations comprising 50 percent or more of the stations in the market, the brokerage agreement could remain in effect for a new owner, for the duration of the initial term of the brokerage agreement. To hold otherwise, as a general matter, could severely and unnecessarily restrict the marketability of stations and station combinations that involve brokerage agreements and seriously undermine the utility of such agreements.[79]

58. The purchaser of a station or stations involved in a brokerage agreement, however, cannot create a new violation or exacerbate an existing violation of our rules by that acquisition. Thus, for example, a station combination that involves a brokerage agreement and that exceeds the 25 percent audience share limit, but is nonetheless permissible under the rules, could not be acquired by a party with another station in the same market. A similar station combination with an audience share of 24 percent could not be acquired by a licensee with a station enjoying a 3 percent share in the same market.

59. Finally, parties will not be permitted to renew or extend time brokerage agreements, including those that are grandfathered, once the initial term expires if, at the time of expiration, the agreement would not be permissible under the rules. The Commission required attribution of time brokerage agreements in order to prevent the use of these agreements to circumvent the revised ownership limits.[80] Allowing the renewal of time brokerage agreements when, for example, the stations' combined audience shares exceed the applicable 25 percent cap, would be tantamount to allowing the entities to have a continuing cognizable ownership interest for an indefinite period of time in stations they could not otherwise own under the local ownership rules.[81] This would be inconsistent with the competition and diversity goals at the heart of the rules. Further, in connection with options to renew or extend time brokerage agreements generally, we reiterate our view that unreasonably long terms in such agreements may call into question a licensee's control of its station.[82]

VI. REMAINING MATTERS

A. Audience Share Benchmark

60. It has been brought to our attention that there is an inconsistency between the language of the *First Reconsideration Order* and that of Section 73.3555(a)(1)(ii) as published, as to the benchmark for permissible audience share. In order to remove any ambiguity on this point, we note that we intended the language of the rule to be controlling. Thus, only audience shares that *exceed* 25 percent are to be considered *prima facie* inconsistent with the public interest.

B. Non-Operational Stations

61. In the *First Reconsideration Order*, the Commission stated that only operating commercial full-power stations would be counted in determining the number of stations in a market, and that non-commercial stations, translators or stations not operational (*i.e.*, stations for which construction permits have been authorized but that are not yet on the air, or stations that have been silent for more than six months) would be excluded.[83] However, we wish to clarify that we did not intend to exclude from consideration under the multiple ownership rules non-operational commercial stations that are part of a transaction or that are commonly owned by a party to the transaction. While it is appropriate to exclude non-operational stations from calculation of the number of stations in the market where we cannot presume that they will add to the competition and diversity in a market, such an analysis is not appropriate when the non-operational station is a part of the transaction under scrutiny, because the applicant has control over and can generally be presumed to intend to put the station on the air. Thus, if the non-operational station is one of the proposed commonly owned stations involved in the transaction, the principal community contour of the non-operational station will not be disregarded in calculating how many stations are counted as in the market or in determining the geographic area for which audience share is calculated.

C. Expanded AM Band

62. In connection with improvements to AM service in MM Docket 87-267, the Commission added Notes 9 and 10 to Section 73.3555 of the Rules.[84] Specifically, Note 9 indicates that an AM licensee may own an existing AM station in the 535-1605 kHz band and apply for a construction permit for an AM station in the expanded band, 1605 kHz-1705 kHz, without regard to otherwise prohibited principal community contour overlap. Moreover, the national ownership restrictions were not applied when an entity with an attributable interest in an AM station in the existing band applies for an AM station in the expanded

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[79] This is not to say that we will ignore concerns of undue market power achieved pursuant to a time brokerage agreement. In the *Report and Order*, we noted that we will carefully review the circumstances through which any station group reaches or exceeds a 40 percent local market share before consenting to a sale of that station group. *Report and Order*, 7 FCC Rcd at 2783 n.109. This qualification is equally applicable to station groups in which one of the attributable interests is a time brokerage agreement.

[80] *Report and Order*, 7 FCC Rcd at 2788.

[81] The Commission stated that if two stations enter into a time brokerage agreement in a market with 15 or more stations and the audience shares subsequently exceed 25 percent of the market, one station may not purchase the other. *First Reconsideration Order*, 7 FCC Rcd at 6402.

[82] *Id.*

[83] *Id.* at 6395.

[84] *Report and Order* in MM Docket No. 87-267 (*Review of the Technical Assignment Criteria for the AM Broadcast Service*), 6 FCC Rcd 6273 (1991), *modified on reconsideration*, 8 FCC Rcd 3250 (1993).

band. Note 10 specifies a five-year period during which joint ownership of existing band and expanded band AM authorizations will be acceptable; at the expiration of this five-year period, the licensee must elect to operate either the expanded band station or to operate the station on its former frequency in the existing band.[85]

63. Consistent with notes 9 and 10, we wish to clarify how joint ownership of existing and expanded band AM stations will be treated if the licensee proposes to acquire another station. If, during the five-year transition period, the licensee has not yet elected whether to move to the expanded band or retain its existing facility, the expanded band station will be disregarded for purposes of the local and national ownership rules. *Report and Order* in MM Docket No. 87-267, 6 FCC Rcd at 6319-20. Thus, the principal community contour of the existing band station will be considered for purposes of determining the relevant market and for purposes of determining the number of stations in the market. Moreover, if it is necessary to determine whether the combination complies with the audience share cap, we will consider only the audience share attributable in the relevant market to the existing band station. We believe this approach will avoid impediments to merger transactions involving expanded band stations that might discourage migration to the expanded band.

VII. ADMINISTRATIVE MATTERS

Regulatory Flexibility Analysis

64. **I. Need for and Purpose of this Action:** This action is taken to address petitions for reconsideration of changes to the Commission's radio multiple ownership rules, and to address a Joint Motion for Rescission and Stay of our national ownership rules. The Commission believes that this action will enhance diversity in the radio industry by providing greater opportunities for minority and small business broadcasters.

65. **II. Summary of Issues Raised by the Public Comments in Response to the Initial Regulatory Flexibility Analysis:** None.

66. **III. Significant Alternatives Considered and Rejected:** The Commission declined to modify its overall national and local multiple ownership rules for radio or to revisit its position regarding time brokerage. The Commission determined that the rules, as modified earlier in this proceeding, are necessary to invigorate the radio industry by permitting greater consolidation of resources. The Commission did modify its national limit with respect to minority and small business owners by (1) adopting a 25 AM/25 FM cap for minorities and (2) increasing to five the number of additional stations in which non-minority broadcasters may take a non-controlling interest, in addition to the general cap, if those stations are controlled by minorities or small businesses.

Effective Date

67. The changes to the rules adopted in this *Memorandum Opinion and Order* will become effective thirty (30) days from the date of publication in the Federal Register.

Additional Information

68. For additional information regarding this proceeding, contact Jane Hinckley Halprin or Alan E. Aronowitz, Mass Media Bureau, Policy & Rules Division, (202) 632-7792, or Melanie Godschall, Mass Media Bureau, Audio Services Division, (202) 418-2660.

VIII. ORDERING CLAUSES

69. IT IS THEREFORE ORDERED that, pursuant to the authority contained in Section 4(i) and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. Section 154(i), 303(r), Part 73 of the Commission's Rules, 47 C.F.R. Part 73. IS AMENDED as set forth in the attached Appendix.

70. IT IS FURTHER ORDERED that the petitions for reconsideration filed in this proceeding ARE GRANTED to the extent indicated herein and ARE DENIED in all other respects.

71. IT IS FURTHER ORDERED that, pursuant to Section 1.401(e) of the Commission's Rules, 47 C.F.R. Section 1.401(e), the Petition for Rule Making filed on August 23, 1993, by the National Association of Broadcasters, RM-8414, IS DENIED.

72. IT IS FURTHER ORDERED that the Joint Motion for Rescission and Stay filed October 7, 1994, by the National Association of Black-Owned Broadcasters and the National Black Media Coalition IS DENIED.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

APPENDIX

Rule Changes

Part 73 of Title 47 of the U.S. Code of Federal regulations is amended to read as follows:

Part 73 RADIO BROADCAST SERVICES

1. The Authority Citation for Part 73 continues to read as follows:

AUTHORITY: 47 U.S.C. 154, 303, 334.

2. Section 73.3555 is amended by deleting paragraphs (a)(3)(iii), and (e)(1)(i), and adding new paragraphs (a)(3)(iii), and (e)(1)(i) to read as follows:

[85] The five-year period begins on the date a construction permit is issued for the new facility in the expanded band. 47 C.F.R. § 73.3555, Note 10.

* * * * *

(a) * * *

(a)(3)(iii) A station's "audience share" is the average number of persons age 12 or older on an average quarter hour basis, Monday-Sunday, 6 a.m.-midnight, who listen to the station expressed as a percentage of the average number of persons listening to AM and FM stations in that radio metro market or a recognized equivalent, in which a majority of the overlap between the same service stations involved in the transaction takes place. The "combined audience share" is the total audience share of all AM or FM stations that would be under common ownership or control following a proposed acquisition. In situations where the majority of the overlap between the same service stations does not lie in a single metro market, the relevant audience share data is the data for all counties that are within the principal community contours of the mutually overlapping stations proposed for common ownership, in whole or in part, weighted based on the listening population, age 12 and older, and totalled to determine the average audience share. Audience share shall be calculated by using the most recent published audience share data available at the time that the application is filed, unless an alternative showing is submitted pursuant to the Note following 47 C.F.R. Sec. 73.3555(a)(1)(ii).

* * * * *

(e) * * *

(e)(1)(i) more than 20 AM or more than 20 FM stations, provided, however, that minority controlled entities may acquire an additional five stations per service above the national limit, and that multiple owners that are not minority-controlled may hold an attributable, but not controlling, interest in five additional stations per service above the national limit that are minority controlled or small business controlled.

* * * * *

SEPARATE STATEMENT

OF

COMMISSIONER ANDREW C. BARRETT

Re: Revision of Radio Rules and policies (MM Docket No. 91-140, RM-8414)

This Order makes certain modifications to our radio ownership rules which I support. In particular, I am encouraged to see additional ownership incentives for minorities and small businesses. However, I remain concerned that allowing minorities and small businesses to own up to 25 AM and 25 FM stations will be an elusive target unless there is greater support from the capital markets for such endeavors.

I also am concerned that our radio ownership report analysis does not specify enough qualitative data regarding the extent to which minority-owned and small stations have benefitted from our relaxed radio ownership rules or local marketing agreements (LMAs). My sense is that they have not benefitted across the board.

I hope that the Commission will seek further data in this regard and make additional adjustments, where necessary, to induce greater flexibility and capital formation support for minority ownership or minority LMA opportunities. I hope we will take up these issues in a further proceeding on minority ownership in the near term.

Before the
Federal Communications Commission
Washington, D.C. 20554

In re:

Cypress Broadcasting, Inc. CSR-3499

Petition for Special Relief

MEMORANDUM OPINION AND ORDER

Adopted: November 21, 1994; Released: November 30, 1994

By the Chief, Cable Services Bureau:

1. Cypress Broadcasting, Inc. ["KCBA-TV"], licensee of Station KCBA-TV (Fox, Channel 35), Salinas, California, has filed a petition for special relief seeking a ruling that KCBA-TV is significantly viewed in Santa Cruz County, California, based on county-wide audience survey data, as opposed to the normally required community-specific data. KCBA-TV's petition is unopposed. Subsequently, Commission staff requested that KCBA-TV update its filing in light of the decisions in *KXTX, Inc.*, 6 FCC Rcd 68 (1991) ["*KXTX*"] and *Nationwide Communications, Inc. (KITN)*, 6 FCC Rcd 52 (1991) ["*KITN*"], and KCBA-TV did so.

2. In 1972, the Commission adopted a comprehensive regulatory scheme for cable television. *Cable Television Report and Order*, 36 FCC 2d 143, *recon.*, 36 FCC 2d 326 (1972). As part of this regulatory scheme, the Commission limited the number of distant signals a cable system could import from outside of its market. Exemptions to these limits, however, were made for both significantly viewed signals and for specialty stations. A signal is considered to be significantly viewed if it meets certain designated minimum viewership levels off-the-air. A station was considered to be a specialty station if it programmed a designated minimum amount of foreign language, religious, or automated programming.[1] When the Commission deleted its distant signal carriage limitations in 1982, the Commission also deleted its rule defining a specialty station. This category of station was no longer needed because there were no longer any rules limiting signal carriage from which exemptions on this basis were needed. *Report and Order in Docket Nos. 20988 and 21284*, 79 FCC 2d 663 (1980), *aff'd sub nom. Malrite TV of New York, Inc. v. FCC*, 652 F.2d 1140 (2d Cir. 1981), *cert. denied*, 454 U.S. 1143 (1982). The Commission continues to utilize the significantly viewed status of signals for various purposes, such as exemption from the Commission's program exclusivity rules. 47 C.F.R. §§76.92(f), 76.156(a). On the other hand, the Copyright Office has continued to recognize specialty station status for purposes of determining royalty payment rates, the carriage of specialty stations by cable systems incurring lesser fees than the carriage of other distant stations. Similar treatment is afforded significantly viewed signals by the Copyright Office.

3. In establishing the category of significantly viewed stations, the Commission published a nationwide list, county-by-county, of those stations initially deemed to be significantly viewed. *Reconsideration of the Cable Television Report and Order*, 36 FCC 2d at 378-463 app. B. Stations not included in this list may be added in one of two ways. A station may demonstrate that it meets the requisite viewership levels utilizing current community-specific data. 47 C.F.R. §76.54(b). Alternatively, a "new" station--one not included in the surveys which established the 1972 list--may utilize county-wide data, provided that such data is from the station's first three years of operations. 47 C.F.R. §76.54(d). For purposes of this rule, the Commission has extended "new" station status to stations shifting from subscription or noncommercial status to commercial status after the initial survey period. *E.g., HR Broadcasting of Milwaukee, Inc. (WCGV-TV)*, Cable Television Actions Report No. 3212 (released April 10, 1989)(STV); *Golden West Broadcasters of Oklahoma, Inc. (KAUT)*, Cable Television Actions Report No. 3110 (released September 8, 1987)(STV); *Blair Broadcasting of Oklahoma, Inc. (KOKH-TV)*, Cable Television Action Report No. 2800 (released October 14, 1983)(noncommercial).

4. KCBA began operation in November 1981, broadcasting religious programming in the early morning, and Spanish-language programming from the late morning until after midnight. KCBA was purchased by its current licensee in 1986. In September of that year, KCBA changed its programming to an English-language news and entertainment format. The station became an affiliate of the Fox Broadcasting Company in April 1987. KCBA contends that it could have been classified as a specialty station at its inception. In view of this, states KCBA, at the time it changed its programming format in September 1986, the station became a "new" station for purposes of determining its status as significantly viewed pursuant to §76.54 of the Rules. KCBA contends that switching its format from specialized to non-specialized programming is similar to a station changing from subscription (STV) or non-commercial to a commercial format, or significantly upgrading its technical facilities, situations in which the Commission has treated a station as "new" for this purpose. In each situation, KCBA maintains, a station of limited audience appeal has made changes in its operation that increase the station's potential viewership. In addition, notes KCBA, the Commission recognized the limited audience appeal of specialty stations in establishing this category, citing the *First Report and Order in Docket No. 20553*, 58 FCC 2d 442, 452, *recon. denied*, 60 FCC 2d 661 (1976).

5. In support of its request to be declared significantly viewed in Santa Cruz County, California, KCBA submits 1989 Nielsen viewing data for this county, which is within the first three years of KCBA's operations in a non-specialty format. According to this data, taken from Nielsen's *1989 County/Coverage Survey, County Summary*, conducted during four separate, consecutive four-week periods in

[1] Former §76.5(kk) of the Rules defined a specialty station as: "A commercial television broadcast station that generally carries foreign language, religious, and/or automated programming in one-third of the hours of an average broadcast week and one-third of weekly prime-time hours."

April-May 1988, July-August 1988, November 1988, and February-March 1989, KCBA achieved in non-cable homes an 11% share of total viewing hours and a net weekly circulation of 46% in Santa Cruz County. Accordingly, states KCBA, it has met the necessary viewership levels to be declared to be significantly viewed as an independent station: a 2% share of total viewing hours and a net weekly circulation of 5%. 47 C.F.R. §76.5(i). Citing *KXTX* and *KITN*, both *supra*, KCBA argues that its change from Spanish-language programming to an English-language format represents a change in the station's basic terms of broadcasting by increasing the number of persons who have access to KCBA's programming. KCBA further argues that, unlike the situations at issue in *KXTX* and *KITN*, in which the petitioning stations had merely altered their program content, KCBA's change from Spanish-language to English-language programming is more substantial. KCBA also notes that its petition is unopposed, unlike the petitions in *KXTX* and *KITN*.

6. As we stated in *Fox Television Stations, Inc.*, 8 FCC Rcd 3213 (1993), we believe that a change from predominantly Spanish- to English-language broadcasting is the sort of fundamental operational change which warrants treating a station as "new" for the purposes of determining its significantly viewed status. Unlike the switch from religious to commercial programming at issue in *KXTX* and *KITN*, a change in language of broadcasting from a specialized to a more common language makes programming suddenly understandable to a far greater audience, who were previously precluded from utilizing the services of the station in question. This change is similar to a station's switching from STV programming to non-scrambled commercial programming, which becomes suddenly viewable by a far greater audience. *Id.* at 3214. Because the audience data submitted by KCBA for noncable homes in Santa Cruz County, California exceeds the Commission's standard for an independent station of a 2% share of total viewing hours and a 5% net weekly circulation, KCBA is entitled to significantly viewed status in Santa Cruz County, California.

7. In view of the foregoing, we find that grant of KCBA's petition is in the public interest.

8. Accordingly, IT IS ORDERED, That the petition for special relief (CSR-3499) filed December 13, 1990, by Cypress Broadcasting, Inc. IS GRANTED.

9. This action is taken by the Chief, Cable Services Bureau, pursuant to authority delegated by §0.321 of the Commission's Rules.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-30

In the Matter of

Amendment of Section 73.606(b),	RM-8457
Table of Allotments,	
TV Broadcast Stations	
(Kaneohe, Hawaii)	

REPORT AND ORDER
(Proceeding Terminated)

Adopted: November 22, 1994; Released: November 30, 1994

By the Acting Chief, Allocations Branch:

1. Pursuant to the request of Collins/West Broadcasting ("petitioner"), the Commission has before it for consideration the *Notice of Proposed Rule Making*, 9 FCC Rcd 1934 (1994), proposing the allotment of UHF Television Channel 66 to Kaneohe, Hawaii, (population 35,448) as that community's first local television service. Petitioner filed comments in support of the proposal reaffirming its intention to apply for the channel, if allotted. HTV/HTN/Hawaiian Television Network, Inc. ("HTVN"), also filed comments stating its intention to apply for Channel 66, if allotted to Kaneohe.

2. We believe the public interest would be served by allotting UHF Television Channel 66 to Kaneohe, Hawaii, since it would provide the community with its first local television service. An engineering analysis has determined that UHF Television Channel 66 can be allotted to Kaneohe consistent with the minimum distance separation requirements of Section 73.610 of the Commission's Rules.[1] However, the allotment of Channel 66 to Kaneohe will require a plus offset.[2] The Commission has imposed a temporary freeze on new television allotments in certain metropolitan areas. However, Kaneohe is not in one of the affected areas.[3]

3. Accordingly, pursuant to the authority contained in Sections (4i), 5(c)(1), 303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61, 0.204(b) and 0.283 of the Commission's Rules, IT IS ORDERED, That effective **January 17, 1995,** the TV Table of Allotments, Section 73.606(b) of the Commission's Rules, IS AMENDED for the community listed below, to read as follows:

City	Channel No.
Kaneohe, Hawaii	66+

4. The window period for filing applications will open on **January 17, 1995**, and close on **February 17, 1995**.

5. IT IS FURTHER ORDERED, That this proceeding IS TERMINATED.

6. For further information concerning this proceeding, contact Nancy J. Walls, Mass Media Bureau, (202) 634-6530. Questions related to the window application filing process should be addressed to the Video Services Division, TV Branch, Mass Media Bureau (202) 418-1630.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

[1] The coordinates for Channel 66 at Kaneohe are North Latitude 21-25-18 and West Longitude 157-48-06.

[2] "A station with a 'plus' or 'minus' offset is required to operate with its carrier frequency 10 kHz above or below the normal carrier frequency. A different offset between two television stations reduces interference and makes possible the separation criteria set forth in our Rules." Crandon, WI, 3FCC Rcd 6765 n.1 (1988).

[3] *See Notice of Inquiry*, 2 FCC Rcd 2125 (1987 and *Order, Advanced Television Systems and Their Impact on the Existing Television Broadcast Service*, 52 FR 28346, July 29, 1987.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

TCI West, Inc. CSR 4337-L

Complaint of Cartographic Publications, Inc.

Leased Access Complaint

MEMORANDUM OPINION AND ORDER

Adopted: November 17, 1994; Released: November 23, 1994

By the Chief, Cable Services Bureau

I. INTRODUCTION

1. On August 2, 1994, Cartographic Publications, Inc. ("Cartographic") filed a Complaint alleging that TCI West, Inc. ("TCI") violated the leased access rules. On September 1, 1994, TCI responded to Cartographic's complaint by filing a motion to dismiss and a request for extension of time to file a response in the event the Commission denied its motion to dismiss. In this Order, the Commission denies TCI's motion to dismiss and grants its motion for extension of time. TCI shall have 10 days from the release of this Order to respond to Cartographic's complaint.

II. BACKGROUND

2. In 1984 Congress enacted as part of an amendment to the Communication Act of 1934 a requirement that cable operators with 36 or more activated channels set aside part of their channel capacity for use by programmers that are not affiliated with them.[1] This requirement is called the leased commercial access requirement. The Cable Television Consumer Protection and Competition Act of 1992 (the "1992 Cable Act"), revisited the leased commercial access requirement and directed the Commission to establish, among other things, procedures for resolving disputes arising from cable operators' leased access requirements.[2] In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket 92-266, 8 FCC Rcd 5631 (1993) (the *"Rate Order")* the Commission followed Congress' directive and established rules governing commercial leased access dispute resolution.[3]

3. The administrative dispute resolution process developed by the Commission pursuant to the 1992 Cable Act is designed to expedite resolution of disputes over leased commercial access requirements. Under this streamlined procedure, any person aggrieved by the failure or refusal of a cable operator to make commercial channel capacity available or to charge rates for such capacity as mandated by the 1992 Cable Act and FCC rules may file a petition for relief with the Commission.[4] The petition must be filed within 60 days of the alleged violation.[5] When a continuing violation is involved, petitions may be filed at any time based on current information. In their petitions, petitioners must concisely state the facts constituting a violation of the 1992 Cable Act or leased access rules and cite the specific statute or rule violated.[6] Petitioners must then serve a copy of the petition on the cable operator. The operator has 30 days from the date the petition is filed to file a response.

4. In addition to the administrative remedy developed by the Commission pursuant to the 1992 Cable Act, the Act expressly provides for judicial review of leased commercial access disputes. Any person aggrieved by the failure or refusal of a cable operator to make channel capacity available for use may bring an action in the district court of the United States for the judicial district in which the cable system is located to compel the cable company to make such capacity available.[7] If the aggrieved party pursues an administrative remedy after a judicial remedy, the Commission will accept a court's finding as sufficient evidence of a violation before the Commission.

III. FACTS

5. Cartographic, a video program distributor, filed a complaint with the Commission on August 1, 1994, pursuant to the administrative commercial leased access dispute resolution provisions at 47 C.F.R. § 76.975. Cartographic's complaint alleges that TCI violated section 612(c)(2) of the Communications Act by, among other things, imposing a scrambling requirement on Cartographic's programming because of its content.[8]

6. Thirty days after Cartographic filed its complaint, TCI filed a Motion to Dismiss the complaint and a Motion for Extension of Time to respond to the complaint. TCI argues for dismissal on the grounds that the Commission does not have jurisdiction to entertain Cartographic's complaint because the Communications Act requires Cartographic to pursue its complaint in federal district court. TCI interprets the Communications Act to require that a complainant sue in a district court if its complaint alleges failure or refusal by a cable operator to make channel capacity avail-

[1] 47 U.S.C. § 532(b)(1)(1992), Communications Act of 1934, § 612(b)(1). The amount of channel capacity an operator must set aside is based on the number of activated channels it has.
[2] 47 U.S.C. § 532(c)(4)(A) & (B) (1992), Communications Act of 1934, § 612(c)(4)(A) & (B).
[3] *Rate Order,* ¶¶531-538. *See also,* 47 C.F.R. § 76.975.
[4] 47 C.F.R. § 76.975(b).
[5] *Id.* at § 76.975(d)
[6] 47 C.F.R. § 76.975(c).
[7] 47 C.F.R. § 76.975(a)
[8] Cartographic states that its programming includes "sexually oriented" content and that it sought to lease channel capacity between midnight and 4 a.m. on various TCI systems. TCI, it alleges, refused to carry Cartographic's programming unless it was scrambled and segregated from other programming and customers were offered an opportunity to affirmatively choose to receive it. Cartographic opposes these requirements and disputes TCI's reliance on 47 C.F.R. § 76.701 as support for them. Cartographic argues that these rules have been stayed by the D.C. Circuit Court of Appeals.

able for leased access use.[9] Under TCI's reading of the statute, the Commission has jurisdiction over leased access disputes only upon a showing of prior adjudicated violation of the leased access provisions by a court.[10] TCI asserts that Cartographic fails to allege an adjudicated violation of the leased access rules in its complaint to the Commission and that, therefore, the Commission is without jurisdiction to hear the complaint.

IV. DISCUSSION

7. The Cable Act's 1992 amendments to the Communication Act's leased access requirement gives the Commission the authority to "establish procedures for the expedited resolution of disputes concerning rates or carriage" under the leased access requirement. § 612 (c)(4)(A)(iii). At the same time, the 1992 Cable Act left in place the provisions of the Communications Act allowing leased access complaints to be filed in U.S. district court and then before the Commission after an adjudication has been made. §§ 612 (d) and (e). These sections were undisturbed by the 1992 amendments.

8. The Commission followed the directive of Congress in the 1992 Cable Act and provided a procedure for resolution of leased access disputes in the *Rate Order*. Section 612(c)(4)(A)(iii) of the Cable Act requires us to establish procedures for the expedited resolution of disputes concerning rates or carriage on leased access channels. The legislative history of Section 612 (c)(4)(A)(iii) indicates that Congress believed that the existing provision of the Cable Act of 1984 entitling aggrieved users to bring action in federal district court or to file complaints at the Commission resulted in procedures that were too cumbersome.[11] The 1992 Cable Act clearly authorized the Commission to develop rules providing for leased access dispute resolution before the Commission as a streamlined procedure. Under this authority the Commission adopted 47 C.F.R. § 76.975 and under this rule, Cartographic filed its leased access complaint against TCI before the Commission.

9. TCI's arguments against the Commission's jurisdiction over Cartographic's complaint are based on the dispute resolution provision of the law prior the 1992 Cable Act. TCI cites only Sections 612 (e) and (d) of the Communications Act and the 1984 legislative history of those provisions. TCI completely ignores developments in the law since 1984. It fails to note the amendment to the Communications Act giving the Commission the authority to make the rules relied upon by Cartographic and it fails to note the legislative history of the 1992 Cable Act that supports the Commission's rules allowing a leased access complaint to be filed with it.[12] The 1992 Cable Act gave parties a new streamlined alternative to the existing procedures for dispute resolution. TCI's arguments in support of its motion to dismiss are without merit. The Commission has jurisdiction over the leased access complaint of Cartographic pursuant to Section 612(c)(4)(A)(iii) of the Cable Act and 47 C.F.R. § 76.975.

10. TCI filed a motion for extension of time to respond to Cartographic's complaint in the event that its motion to dismiss was denied. TCI states in that motion that it is prepared to respond to the merits of Cartographic's complaint expeditiously if the Commission denies its motion to dismiss. Because we deny TCI's motion to dismiss, we will grant its request for an extension of time to file a response to the leased access complaint of Cartographic and hereby grant TCI 10 days from the release of this order to file its response as required by rule 47 C.F.R. § 76.975.

V. ORDERING CLAUSE

11. Accordingly, IT IS ORDERED that TCI West, Inc.'s motion to dismiss the complaint of Cartographic Publications, Inc. is hereby DENIED,

12. IT IS FURTHER ORDERED that TCI West Inc.'s motion for extension of time to file a response to the complaint of Cartographic Publications, Inc. is hereby GRANTED and TCI West, Inc. must file its response within 10 days from the release of this order,

13. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

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[9] TCI cites 47 U.S.C. § 532(d).
[10] TCI cites 47 U.S.C. § 532(d).
[11] *Rate Order*, at ¶53 1.
[12] *See*, H.R. 4580 committee Report (Rpt. 102-628), pp. 39-40 (The cumbersome enforcement mechanism. . . may explain why some cable operators cite very low demand for leased access channels.)

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

CENTURY SOUTHWEST
CABLE TELEVISION CORP.,

- Petition for Stay of Local
Rate Order of Beverly Hills, CA

COMCAST CABLEVISION
OF MOUNT CLEMENS, INC.

- Request for Stay of Local
Rate Order of Mount Clemens, MI

COMCAST CABLEVISION
OF TALLAHASSEE, INC.

- Request for Stay of Local
Rate Order of Tallahassee, FL

LONG BEACH
ACQUISITION CORP., d/b/a
CABLEVISION INDUSTRIES

- Petition for Stay of Local
Rate Order of Long Beach, CA

CENTURY CABLE OF
SOUTHERN CALIFORNIA

- Petition for Stay of Local
Rate Order of Brea, CA

CENTURY CABLE OF
SOUTHERN CALIFORNIA

- Petition for Stay of Local
Rate Order of La Habra, CA

LONG BEACH
ACQUISITION CORP., d/b/a
CABLEVISION INDUSTRIES

- Petition for Stay of Local
Rate Order of Signal Hill, CA

WARNER CABLE
COMMUNICATIONS, INC.

- Petition for Stay of Local
Rate Order of Wadsworth, OH

CONSOLIDATED ORDER

Adopted: November 18, 1994; Released: November 22, 1994

By the Chief, Cable Services Bureau:

1. Over the course of the past several months, we have granted and, in some cases, extended eight stays of local rate orders in which the length of the stays was specifically tied to resolution of Letters of Inquiry ("LOIs") issued by the Commission in the latter part of 1993 and earlier this year.[1] Each of the local rate orders had established rates for basic service and directed the operators to issue refunds after concluding that a la carte packages offered by the operators were subject to rate regulation. By this Consolidated Order, and on our own motion, we hereby clarify the terms of those eight stay orders. The clarification will address any uncertainty regarding the termination date of those stay orders that might otherwise exist as we begin to issue orders on the pending LOIs.

2. In four of the eight cases, we have issued LOIs with respect to the a la carte packages provided by the particular operators.[2] The language we used to define the terms of the stay issued in the *Comcast, Tallahassee, Florida* case was typical.[3] There we granted the stay "until the earlier of a date ten (10) days after the release of an Order or Orders by the Commission finally resolving the issues raised in the Letter of Inquiry to Comcast or the resolution of the instant appeal."[4] We are now of the view that the release of orders through the LOI process may not address all outstanding issues on appeal. In addition, the a la carte packages under review in the LOI process may not completely resolve the a la carte issue raised by the appeals.

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[1] *See Century Southwest Cable Television Corp.* (Beverly Hills, CA), DA 94-463 (rel. May 9, 1994); *Comcast Cablevision of Mount Clemens* (Mt. Clemens, MI), DA 94-857 (rel. Aug. 9, 1994); *Comcast Cablevision of Tallahassee, Inc.* (Tallahassee, FL), DA 94-1071 (rel. Sept. 30, 1994); *Long Beach Acquisition Corp., d/b/a Cablevision Industries* (Long Beach, CA), DA 94-1212 (rel. Nov. 7, 1994); Century Cable of Southern California (Brea, CA), DA 94-860 (rel. Aug. 9, 1994); *Century Cable of Southern California* (La Habra, CA), DA 94-859 (rel. Aug. 9, 1994); *Long Beach Acquisition Corp., d/b/a Cablevision Industries* (Signal Hill, CA), DA 94-1213 (rel. Nov. 7, 1994); *and Warner Cable Communications, Inc.* (Wadsworth, OH), DA 94-858 (rel. Aug. 9, 1994). Three groups of LOIs were issued to cable operators on November 17, 1993, December 13, 1993, and February 22, 1994, in which we asked certain cable operators to provide information concerning various rate and service changes and practices. Many of the LOIs requested information involving a la carte offerings.

[2] *See Century Southwest Cable Television Corp.* (Beverly Hills, CA), DA 94-463 (rel. May 9, 1994); *Comcast Cablevision of Mount Clemens* (Mt. Clemens, MI), DA 94-857 (rel. Aug. 9, 1994); *Comcast Cablevision of Tallahassee, Inc.* (Tallahassee, FL), DA 94-1071 (rel. Sept. 30, 1994); *and Long Beach Acquisition Corp., d/b/a Cablevision Industries* (Long Beach, CA), DA 94-1212 (rel. Nov. 7, 1994).

[3] *Comcast Cablevision of Tallahassee, Inc.* (Tallahassee, FL), DA 94-1071 (rel. Sept. 30, 1994).

[4] *Id.*

3. We have not issued LOIs to the other operators.[5] Despite the absence of LOIs in those cases, we granted those stay requests pending resolution of the a la carte issue in the LOI context generally or, alternatively, pending resolution of the specific appeal. The language we used in the *Warner, Wadsworth, Ohio* stay decision was typical.[6] There we granted the stay "until the earlier of a date ten (10) days after the release of an Order or Orders by the Commission finally resolving the issues raised in the Letters of Inquiry or the resolution of the instant appeal."[7] We took this approach on the expectation that resolution of one or more of the LOIs issued to other operators would provide the necessary guidance to the operators and communities in these cases to enable them to resolve their differences over the a la carte packages. For the reasons identified in paragraph 2, *supra,* we believe that these stays should be clarified and extended as well.

4. In order to reduce any possible uncertainty regarding the termination date of each of the eight stay orders, we are extending the stays issued in each case until we release orders resolving each operator's appeal.

5. Accordingly, on our own motion, IT IS ORDERED, that our decisions, which previously granted stay requests in *Century Southwest Cable Television Corp.* (Beverly Hills, CA), DA 94-463 (rel. May 9, 1994); *Comcast Cablevision of Mount Clemens* (Mt. Clemens, MI), DA 94-857 (rel. Aug. 9, 1994); *Comcast Cablevision of Tallahassee, Inc.* (Tallahassee, FL), DA 94-1071 (rel. Sept. 30, 1994); *Long Beach Acquisition Corp., d/b/a Cablevision Industries* (Long Beach, CA), DA 94-1212 (rel. Nov. 7, 1994); *Century Cable of Southern California* (Brea, CA), DA 94-860 (rel. Aug. 9, 1994); *Century Cable of Southern California* (La Habra, CA), DA 94-859 (rel. Aug. 9, 1994); *Long Beach Acquisition Corp., d/b/a Cablevision Industries* (Signal Hill, CA), DA 94-1213 (rel. (Nov. 7, 1994); *and Warner Cable Communications, Inc.* (Wadsworth, OH), DA 94-858 (rel. Aug. 9, 1994) are hereby amended to provide that each local rate order is STAYED pending the Commission's resolution of the operator's appeal.

6. This action is taken by the Chief, Cable Services Bureau, pursuant to authority delegated by Section 0.321 of the Commission's rules. 47 C.F.R § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[5] *See Century Cable of Southern California* (Brea, CA), DA 94-860 (rel. Aug. 9, 1994); *Century Cable of Southern California* (La Habra, CA), DA 94-859 (rel. Aug. 9, 1994); *Long Beach Acquisition Corp., d/b/a Cablevision Industries* (Signal Hill, CA), DA 94-1213 (rel. Nov. 7, 1994); *and Warner Cable Communications, Inc.* (Wadsworth, OH), DA 94-858 (rel. Aug. 9, 1994).

[6] *Warner Cable Communications, Inc.* (Wadsworth, OH) , DA 94-858 (rel. Aug. 9, 1994).

[7] *Id.*

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Mid-Atlantic CATV Limited Partnership — CUID No. MD0355 (Howard County, MD)

Cost of Service Filing To Support Cable Programming Service Rate

MEMORANDUM OPINION AND ORDER

Adopted: November 8, 1994; Released: November 9, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On May 23, 1994, Mid-Atlantic CATV Limited Partnership ("Mid-Atlantic") filed a cost of service submission with the Commission in response to complaints that allege that Mid-Atlantic's cable programming service ("CPS") rate in its Howard County, Maryland franchise is excessive.[1]

2. Mid-Atlantic's cost of service filing seeks to establish that its CPS rate of $22.05 per month for the period September 1, 1993, to May 14, 1994, is justified based on Mid-Atlantic's cost of providing CPS. Our review of the record indicates that, although not all of the costs in Mid-Atlantic's showing are allowable under general cost of service principles, even if we disallow those non-allowable costs, Mid-Atlantic's CPS rate in effect for the referenced time period is justified under cost of service principles.[2]

3. According to information provided by Mid-Atlantic in its cost of service submission, its system provides service to approximately 2,989 basic subscribers and 2,923 CPS subscribers. Mid-Atlantic provides 22 channels on its basic tier and 30 channels on its CPS tier.

4. We emphasize that in this review process, pursuant to the 1992 Cable Act, we are analyzing rates for a limited past period, solely for the purpose of determining whether any refund liability has arisen.[3] As discussed below, we are applying general cost of service principles with Commission rules and guidance that were available at the time these filings were made.

II. BACKGROUND

5. On May 3, 1993, the Commission released its *Rate Order* establishing rules to implement the cable television rate regulation provisions of the 1992 Cable Act. In the *Rate Order*, the Commission determined that a benchmark and price cap approach should serve as the primary method for regulating basic service and CPS rates. The Commission also concluded that because the benchmark methodology might not produce fully compensatory rates in all cases, it was appropriate to permit operators, as an alternative, to justify rates based on costs, using individual cost of service showings.[4] The cost of service approach was intended to be used only if an operator believed that the maximum rate permitted under the benchmark formula would not enable the operator to recover costs reasonably incurred in providing rate regulated cable services.

6. The Commission found, however, that the record before it at the time of the adoption of the *Rate Order* did not provide sufficient information on which to develop detailed cost of service rules for the cable industry.[5] Therefore, on July 16, 1993, the Commission issued a Notice of Proposed Rulemaking which proposed requirements to govern cost of service showings submitted by cable operators seeking to justify rates higher than those determined under the benchmark approach.[6] The Commission indicated in the *Notice*, as it did in the *Rate Order*, that general cost of service principles would apply to cost of service filings submitted prior to the adoption of specific rules.[7] Mid-Atlantic's cost of service filing under review here was submitted during that pre-adoption time period and covers only the period prior to May 15, 1994. We are analyzing the rates in effect for the period prior to May 15, 1994, as the Commission instructs, under general cost of service principles, not under the rules adopted by the Commission in February 1994.[8]

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[1] The earliest of the complaints to which Mid-Atlantic responds was served on Mid-Atlantic on November 22, 1993. Pursuant to 47 C.F.R. § 79.956, Mid-Atlantic was required to respond to the complaints within 30 days of service, thus establishing December 21, 1993 as Mid-Atlantic's filing deadline with respect to that complaint. We are accepting Mid-Atlantic's late-filed response pursuant to our *May 23 Order*. Cable Operators' Rate Justification Filings, Sections 76.945, 76.956 of the Commission's Rules, Order, DA 94-526 (released May 23, 1994) ; *see also*, Cable Operators' Rate Justification Filings, Order, DA 94-619 (released June 14, 1994).

[2] This Order does not make any findings or rulings regarding Mid-Atlantic's rates for basic service and equipment, or premium services. Regulation of rates for basic service and equipment is generally the responsibility of the local franchising authorities, and premium services are unregulated. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) (*"Rate Order"*), at 5637. Data for these services were reviewed only to the extent needed for our evaluation of the reasonableness of an operator's CPS rates.

[3] *See* Communications Act of 1934, as amended by the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act"), at § 623(c)(1)(C). The 1992 Cable Act authorizes the Commission to order that the operator refund to subscribers that portion of rates that subscribers have paid after the filing of a valid complaint, that are then found to be unreasonable.

[4] Rate Order, 8 FCC Rcd at 5794-95; *see also*, 47 C.F.R. §76.922.

[5] *Rate Order*, 8 FCC Rcd at 5798-99.

[6] Implementation of Sections of the Cable Television Consumer Protection Act of 1992: Rate Regulation, MM Docket No. 93-215, Notice of Proposed Rulemaking, FCC 93-353, released July 16, 1993, 58 Fed. Reg. 40762 (July 30, 1993) (*"Notice"*).

[7] *Id.* at 40763; *Rate Order*, 8 FCC Rcd at 5798-99, 5854, n.859.

[8] In February 1994, the Commission adopted an order setting forth specific regulatory requirements to govern cost of service

III. DISCUSSION

7. In analyzing Mid-Atlantic's cost of service submission, we considered that the cost of service approach permits rates to be set to allow a company to recover the reasonable costs of providing rate regulated cable services, including an opportunity to earn a fair return on its investment.[9] If we find that a certain rate base or expense element is not supported, is excessive, or is unrelated to providing rate regulated cable service, we can disallow that cost in whole or in part.[10] We have evaluated rate base and expense items to determine whether Mid-Atlantic should be permitted to recover those items in its rates. In some cases, we have found costs that are not allowable, and we have made appropriate adjustments. Even with our adjustments and disallowances, however, we find that Mid-Atlantic's CPS rate for the period under review has been justified.

8. ***Rate Base:*** *Rate base represents the amount of investment the cable company makes in its facilities to provide service to its customers. Under traditional cost of service principles, it is necessary to determine the allowable rate base in order to calculate the revenue requirement based on the applied rate of return. In analyzing Mid-Atlantic's filing, we reviewed the components of Mid-Atlantic's rate base to determine the investment upon which Mid-Atlantic is entitled to earn a return. For purposes of this review, we made adjustments to the rate base as discussed below.*

(a) *Operating Losses:* Mid-Atlantic proposes to include start-up losses of $1,079,185 in its rate base, of which $625,927 had been allocated to the CPS portion of the rate base. For this review we are allowing operating losses accumulated over the prematurity period as defined by Statement of Financial Accounting Standards No. 51, Financial Reporting by Cable Television Companies ("FAS 51").[11] Under FAS 51, the prematurity phase of a cable television system is presumptively no longer than two years, although it may arguably be longer. Mid-Atlantic did not provide any argument that its prematurity period was longer than two years. Accordingly, for purposes of this analysis the recovery of accumulated start-up losses in Mid-Atlantic's rate base is limited to two years.

(b) After reviewing Mid-Atlantic's filing, we were unable to determine what portion of the $625,927 represents the system's first two years of start-up losses because it did not specify that the start-up losses reported are limited to the losses incurred in the first two years. It indicated, however, that cable service was inaugurated in 1989, and it is possible, therefore, that the losses claimed in Mid-Atlantic's filing reflect losses for a five-year period beginning in 1989. Using this worst case assumption, we have calculated Mid-Atlantic's start-up losses for the first two years as $151,085, net of accumulated amortization. We adjusted the rate base to disallow 60% (three of the five years' worth) of the claimed start-up losses and related accumulated amortization expense. Therefore, the following adjustments were made:

	Mid-Atlantic Proposed	Commission Adjustment[12]	Allowable Start-up Losses
Start-up Losses	$625,927	($410,090)	$215,837
Accum. Amortization (Start-up Losses)	($354,756)	$290,004	($64,752)
Total	$271,171	($120,086)	$151,085

(c) *Allocation:* The Commission's rules in effect at the time of Mid-Atlantic's filing clearly specify that tier allocations are to be made based on the ratio of channels on each tier to the total number of channels offered.[13] In allocating most of its rate base, Mid-Atlantic used the allocator of "ratio of channels on basic service . . . and CPS tiers to the sum total of [basic service] and CPS channels." While this allocator is channel-based, it is inappropriate because it distributes the rate base to only two of Mid-Atlantic's three service tiers. It does not allocate a portion of rate base to the unregulated tier, Other Programming Services Activities ("OPSA"), which certainly uses the facilities included in the rate base accounts. Mid-Atlantic's allocator does not comply with the

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filings to justify rates above levels determined under its benchmark requirements. The new rules apply to rates charged or to be charged after May 15, 1994. *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd 4527 (1994) (*"Cost Order"*).

[9] *See Notice* at 40765:

> Under traditional cost-of-service regulation, rates are set at a level to provide the company with recovery of its costs and a reasonable opportunity to earn a fair return on its invested capital. Under the traditional formulation, the company's revenue requirement is equal to the expenses of providing service and its return on investment.

[10] The Commission made clear that the fact that an operator has incurred costs does not necessarily establish its right to recover those costs from subscribers. *See Rate Order*, 8 FCC Rcd at 5794, n.619. "When electing [to make] a cost of service showing, the cable operator assumes the risk that its rate could be lowered if such action is justified by the cost showing." *Id.* at 5800, para. 272.

[11] FAS 51 establishes standards of financial accounting and reporting for costs, expenses, and revenues applicable to the construction and operation of cable television systems. These standards are considered to be generally accepted accounting principles, and provide guidance as "general cost of service principles," in the absence of specific rules. Under these standards, when a cable system is partially under construction and partially in service (the prematurity period), costs incurred that relate to both current and future operations shall be partially capitalized as start-up costs and partially expensed.

[12] Our adjustment includes an allocation of start-up losses based on the ratio of channels on each tier to the sum total of all channels offered (including those on non-regulated tiers). As discussed in detail below in para. (c), this allocation method is the appropriate method pursuant to the Commission's rules in effect at the time of Mid-Atlantic's filing.

[13] *See Rate Order*, 8 FCC Rcd at 5976. *See also*, 47 C.F.R. § 76.924(e)(2). Costs allocated to the franchise level must be allocated between tiers in proportion to the number of channels on each tier. This requirement does not apply to programming costs, franchise fees, or public, educational and government access costs, which are allocated entirely to the basic tier or directly assigned as appropriate.

requirement that allocations be based on the ratio of channels on each tier to the total number of channels offered, and the failure to allocate rate base to OPSA results in an overstatement of the revenue requirement for both the basic service and CPS tiers. Accordingly, we have applied the appropriate allocator (the ratio of channels on each tier to the sum total of all channels offered) to Mid-Atlantic's analysis, resulting in the following adjustments:

Account	Mid-Atlantic Proposed	Commission Adjustment	Allowable Allocation Amount
Trunk and Distribution Facilities	$2,171,143	($289,486)	$1,881,657
Drops	$ 753,996	($100,533)	$ 653,463
Organizational and Franchise Costs	$ 350,672	($ 48,369)	$ 302,303
Accumulated Amortization	($ 162,000)	$ 49,977	($ 112,023)

(e) For the following rate base accounts, Mid-Atlantic allocated 10% of the expense to the equipment basket and the remainder to its basic and CPS tiers in the manner discussed above (i.e., on the basis of the ratio of channels on basic service and CPS tiers to the sum total of basic service and CPS channels). For the reasons discussed above, Mid-Atlantic's allocation methodology is inappropriate because it fails to allocate to the OPSA tier. We, therefore, have reallocated the following accounts by allowing the 10% allocation to the equipment basket, but allocating the remaining balances using the appropriate allocator, the ratio of channels on each tier to the sum total of all channels offered (including non-regulated channels). This resulted in the following adjustments:

Account	Mid-Atlantic Proposed	Commission Adjustment	Allowable Allocation Amount
Constru/Main. Facil. and Equip.	$38,897	($1,639)	$37,258
Business Office Facil. and Equip.	$40,098	($5,531)	$34,567

(f) In allocating the Accumulated Depreciation, Mid-Atlantic used the allocator of "ratio of plant assets by category." As explained above, however, the Commission's rules in effect at the time of Mid-Atlantic's filing require that allocations be based on the ratio of channels on each tier to the total number of channels offered. We, therefore, reallocated Accumulated Depreciation using such an appropriate allocator, resulting in the following adjustment:

Account	Mid-Atlantic Proposed	Commission Adjustment	Allowable Allocation Amount
Accumulated Depreciation	($659,608)	$36,230	($623,378)

9. ***Rate of Return:*** *A regulated entity is entitled to the opportunity to earn a fair return on investment.*[14] *That return should be sufficient to ensure confidence in the financial integrity of the enterprise,*[15] *but should be balanced against our interest in protecting a company's subscribers from paying excessive rates. In the Rate Order* the Commission stated that it would make a case-by-case determination of reasonableness for submissions made before specific cost rules could be adopted.[16] In the rulemaking notice initiating a proceeding to adopt such rules, released several weeks before the submission date of these initial cost of service filings, the Commission discussed its analysis of rate of return generally, and tentatively concluded that an after-tax, overall rate of return in the range of 10-14% would reflect a reasonable balancing of subscriber and cable operator interests.[17] In the *Notice*, the Commission reached its tentative conclusion of a range of reasonableness from 10-14% based on a summary analysis of the cost of equity and the capital structure of regulated cable services.[18] The *Rate Order* postulated a case-by-case determination of reasonableness regarding the rate of return. As a general approach for evaluation of refund liability from cost of service showings submitted before the effective date of the cost of service rules, we find it appropriate and reasonable to make reference to the range discussed in the *Notice* for our analysis, and to determine the reasonableness of the proffered return in light of that range and of other evidence presented. Mid-Atlantic uses a rate of return of 11.25%, which we find reasonable. Thus, we have made no adjustments in this regard.

10. **Operating Expenses:** Cable operators may recover in rates their reasonable operating expenses normally associated with providing rate regulated cable services. Our review of Mid-Atlantic's operating expenses under general cost of service principles results in adjustments as discussed below:

(a) *Out-of-period Adjustments:* Mid-Atlantic made certain out-of-period adjustments to its test year balances. These adjustments were not supported by explanations of the reasons for such adjustments or explanations of the methodology used and source data compiled in making the adjustments. We find, therefore, that Mid-Atlantic has not provided the requisite support for its post test year adjustments. As a result, we eliminated the post test year adjustments to the Cable Payroll, Pole Rental, Program Acquisition,

[14] *Notice* at 40769.

[15] *Id.; see also, Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 603 (1944).

[16] *Rate Order*, 8 FCC Rcd at 5795, para. 264.

[17] *See Notice* at 40765. Since the release of the *Notice*, the Commission has adopted a unitary rate of return for cable of 11.25%. *Cost Order*, 9 FCC Rcd at _____, para. 147. The Commission adopted the 11.25% rate of return on an interim basis, based on evidence in the record. However, the *Cost Order* applies to rate justification filings submitted after the effective date of the rules, and not to filings already pending. *Id.* at 4527, para. 5; *see also, Rate Order*, 8 FCC Rcd at 5854, n.859.e

[18] *See Notice* at 40765.

General and Administrative, and Management Fees accounts. This resulted in a total adjustment to Mid-Atlantic's revenue requirement of $91,211.

(b) *Amortization Expense:* The disallowance of excess start-up losses in Mid-Atlantic's rate base, as discussed above, necessitates an adjustment to Mid-Atlantic's claimed amortization expense related to start-up losses. Mid-Atlantic proposes to amortize its start-up losses ($625,927) over a ten-year period, resulting in an annual amortization expense of $62,593. According to generally accepted accounting principles, capitalized start-up losses are to be amortized over the same period used to depreciate the main cable television plant.[19] We believe this is the appropriate standard for the amortization allowance for start-up losses recoverable in regulated charges. Mid-Atlantic uses a useful life of ten years for its main cable plant. We, therefore, conclude that the ten-year amortization period is reasonable, and we have amortized the allowable start-up losses of $215,837 (as determined above) over that ten-year period. This results in an allowable annual amortization expense of $21,584 and, therefore, a disallowance of $41,009 ($62,593 - $21,584).

(c) *Allocation:* As with the rate base items discussed above, Mid-Atlantic inappropriately allocated certain operating expenses by using an allocator based on the ratio of basic service and CPS channels to the sum total of basic service and CPS channels. As discussed above, this allocator does not comply with the Commission's rules in effect at the time of Mid-Atlantic's filing that require that allocations be based on the ratio of channels on each tier to the sum total of all channels offered (including non-regulated channels). Accordingly, we have applied the appropriate allocator (the ratio of channels on each tier to the sum total of all channels offered, which includes OPSA) to Mid-Atlantic's analysis, resulting in the following adjustments:

Account	Mid-Atlantic Proposed	Commission Adjustment	Allowable Allocated Amount
Cable Plant Power Expense	$33,631	($4,639)	$28,992
Pole Rental and Other Rentals	$38,554	($7,244)	$31,310
Amortization Expense-Franch.,Org. Costs	$41,019	($5,658)	$35,361

(d) For the following operating expense accounts, Mid-Atlantic allocated 5% of the expense to the equipment basket and the remainder to its basic and CPS tiers on the basis of the ratio of channels on basic service and CPS tiers to the sum total of basic service and CPS channels. For the reasons discussed above, Mid-Atlantic's allocation methodology is inappropriate because it fails to allocate to the OPSA tier. We, therefore, have reallocated the following accounts by allowing the 5% allocation to the equipment basket, but allocating the remaining balances using the appropriate allocator, the ratio of channels on each tier to the sum total of all channels offered (including non-regulated channels). This resulted in the following adjustments:

Account	Mid-Atlantic Proposal	Commission Adjustment	Allowable Allocation Amount
Cable Plant Employee Payroll	$133,979	($22,419)	$111,560
General & Admin. Expenses	$ 59,266	($14,071)	$ 45,195
Operating Taxes	$ 29,284	($ 3,525)	$ 25,759

11. Income Tax Allowance: Mid-Atlantic calculated its income tax allowance using a methodology that added Mid-Atlantic's state and federal income tax rates together. This methodology is incorrect because it does not take into account the deductibility of federal income taxes in Mid-Atlantic's calculation of its state income tax expense. Mid-Atlantic's method results in the inclusion of more than Mid-Atlantic's actual tax expenses, and, thus overstates its revenue requirement. We, therefore, adjusted Mid-Atlantic's tax allowance by using a methodology that properly accounts for the deductibility of the federal income taxes, resulting in an adjustment of ($56,656) to the $125,054 tax allowance included by Mid-Atlantic.

[19] *See* Statement of Financial Accounting Standards No. 51, Financial Reporting by Cable Television Companies, FAS 51, para. 10.

IV. CONCLUSION

12. Based on our review of Mid-Atlantic's cost of service filing, applying general cost of service principles and applicable allocation rules, we find that, while Mid-Atlantic's cost of service showing overstates its revenue requirement, Mid-Atlantic's CPS rate for the period under review, $22.05, is justified based on this showing.[20]

13. Accordingly, IT IS ORDERED, pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321, that the CPS rate charged by Mid-Atlantic CATV Limited Partnership with respect to the above-referenced CUID number, for the period September 1, 1993, to May 14, 1994, of $22.05 is justified under general cost of service principles, and no refund liability for CPS services during that period will be imposed.[21]

14. IT IS FURTHER ORDERED that the complaints filed against Mid-Atlantic CATV Limited Partnership regarding its CPS rate for the period September 1, 1993, to May 14, 1994, ARE DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[20] This finding is based solely on the representations of Mid-Atlantic in its cost of service filing. Should information come to our attention that these representations (including representations as to the status of *a la carte* packages or data regarding installations and customer equipment) were materially inaccurate, we reserve the right to take appropriate action. This Order is not to be construed as a finding that we have accepted as correct any specific entry, explanation or argument made by any party to this proceeding not specifically addressed herein (including the operator's Form 393).

[21] The findings in this Order do not in any way prejudge the reasonableness of prices for CPS service after May 14, 1994 under our rate regulations. However, to the extent Mid-Atlantic has sought to take advantage of the refund deferral period under the *Second Order on Reconsideration* (Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, 9 FCC Rcd 4119 (1994)), the CPS rate found reasonable herein might also apply from May 15, 1994 until the date on which Mid-Atlantic implemented its CPS price under the new regulations.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

TELESYSTEMS OF	Cheshire, CT
CONNECTICUT, INC., d/b/a	Meriden, CT
DIMENSION CABLE SERVICES	Southington, CT

Petition for Stay of Local
Rate Order of the Connecticut
Department of Public Utility Control

ORDER

Adopted: November 21, 1994; Released: November 23, 1994

By the Chief, Cable Services Bureau:

1. Telesystems of Connecticut, Inc., d/b/a Dimension Cable Services ("Dimension") filed on September 9, 1994, a Petition for Stay Pending Review ("Petition") of the local rate order ("Local Rate Order") adopted by the Connecticut Department of Public Utility Control ("DPUC") on August 10, 1994.[1] The DPUC did not submit any pleadings in opposition to Dimension's Petition. The Local Rate Order establishes a new rate schedule for Dimension's basic service tier and cable service installations, and directs Dimension to issue refunds to subscribers for those charges it assessed between September 1, 1993 and July 14, 1994 which were in excess of the newly established rates.[2] The main issue raised by Dimension in its Petition centers on the proper regulatory treatment of Dimension's a la carte package offerings.

2. The Commission has issued numerous Letters of Inquiry ("LOI") to cable operators regarding the regulatory treatment of a la carte package offerings. On December 13, 1993, the Commission issued three (3) such LOIs to Times Mirror Cable Television, Inc. ("Times Mirror"), Dimension's parent company.[3] Given that Dimension's Petition presents the same issues as those raised in the LOIs issued to Times Mirror, and in order to minimize subscriber confusion and ensure regulatory consistency pending resolution of the Commission's LOIs, we shall grant Dimension's Petition.[4] The Local Rate Order shall be stayed pending the resolution of Dimension's Appeal.

3. During the period of this stay, Dimension is ordered to deposit in an interest-bearing escrow account the total amount of money that the DPUC has ordered Dimension to refund to its customers. Alternatively, Dimension may elect to post a bond for the benefit of the DPUC.[5] The amount of the bond shall be the total amount of money subject to the refund order, plus interest on that amount for a twelve (12) month period from the date of this Order. The bond shall provide that if Dimension is unable to fulfill its refund obligations for any reason, then the surety will fulfill that obligation to the DPUC, on behalf of Dimension's subscribers.

4. Accordingly, IT IS ORDERED that the Local Rate Order adopted by the DPUC is STAYED pending the resolution of Dimension's Appeal.

5 . IT IS FURTHER ORDERED that the amount of the refunds required by the DPUC's Local Rate Order SHALL BE PLACED by Dimension in an interest-bearing escrow account, OR SHALL BE SECURED by the posting of a bond for the benefit of the DPUC for the amount of money the DPUC has ordered Dimension to refund, plus interest. The amount of the bond shall be the total amount of money subject to the refund order, plus interest on that amount for a twelve (12) month period from the date of this Order. Proof of Dimension's compliance with this Order shall be filed with the Commission within thirty (30) days of the release of this Order. Interest shall accrue, or be computed, at the prevailing U.S. Internal Revenue Service Rate.

6. This action is taken by the Chief, Cable Services Bureau, pursuant to authority delegated by Section 0.321 of the Commission's rules. 47 C.F.R. §0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones

Chief, Cable Services Bureau

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[1] Dimension also filed a Petition for Review ("Appeal") of the DPUC's local rate order on September 9, 1994. The DPUC filed an Opposition to Dimension's Appeal ("Opposition") on September 22, 1994. Dimension filed a Reply to the DPUC's Opposition on October 6, 1994.

[2] Under the Cable Television Consumer Protection and Competition Act of 1992 and the Commission's implementing regulations, local franchising authorities may regulate rates for basic cable service, associated equipment and installations. See Cable Television Consumer Protection and Competition Act, Pub. L. No. 102-385, 106 Stat. 1460 (1992); Communications Act, § 623(b), *as amended*, 47 U.S.C. § 543(b) (1993).

[3] Petition, at 3.

[4] See *Paragon Cable* (Grapevine, TX), DA 94-1072 (Rel. September 30, 1994); *Century Cable Management Corporation* (East Haddam, CT, et. al.), DA 94-1110 (Rel. October 6, 1994); *Century Norwich Corporation* (Bozrah, CT, et. al.), DA 94-1111 (Rel. October 6, 3-1994); and *Time Warner Entertainment Company, L.P., d/b/a Laurel Cablevision* (Litchfield, CT, et. al.), DA 94-1112 (Rel. October 6, 1994).

[5] See *Comcast Cablevision of Tallahassee, Inc.*, DA 94-1071 (Rel. September 30, 1994), in which the Commission authorized the operator to post a bond in lieu of establishing an escrow account. See, also *Paragon Cable; Century Cable Management Corporation; Century Norwich Corporation;* and *Time Warner Entertainment Company, L.P., d/b/a Laurel Cablevision.*

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

STAR CABLE ASSOCIATES

Petition for Reconsideration
of the Certification of
Floyd County, Virginia
to Regulate Basic Cable Rates
(VA0422)

MEMORANDUM OPINION AND ORDER

Adopted: November 22, 1994; Released: November 23, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On December 13, 1993, Star Cable Associates ("Star Cable") filed a timely petition for reconsideration challenging the certification of Floyd County, Virginia to regulate rates for basic cable service and associated equipment.[1] Floyd County did not file an opposition to Star Cable's petition.

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[2] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[3] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[4] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[5] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[6]

II. DISCUSSION

3. Star Cable argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in the unincorporated areas of Floyd County, its franchise area.[7] Star Cable claims that it currently serves only 138 of the 4,567 households (that is, occupied housing units)[8] in its franchise area, or 3 percent of the total number of households. As supporting documentation, Star Cable provides 1990 Census data[9] which shows that there are 4,567 households in the unincorporated areas of Floyd County. Star Cable also submits a computer print-out with sufficient subscriber information to support its claim that it serves 138 households in the franchise area. Finally, Star Cable provides an affidavit by a responsible official certifying the accuracy of the data included in the petition.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[10] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[11] Star Cable has met this burden. Star Cable appropriately relied on data reflecting the number of households as required by our rules.[12] Relying on this data, Star Cable has submitted sufficient evidence demonstrating that its cable system serving Floyd County, its franchise area, serves 138 of the 4,567 households, or 3 percent of the households, within its franchise area. Thus, we find Star Cable's system serving Floyd County is subject to effective competition. Accordingly, its petition is granted.

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[1] Floyd County filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on October 18, 1993, which became effective on November 17, 1993.

[2] 47 U.S.C. § 543(a)(4).

[3] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[4] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition. 47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[5] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[6] 47 C.F.R. § 76.911(c).

[7] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[8] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 6-4316, 4324 (1994) (*"Third Recon. Order"*). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[9] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994).

[10] 47 C.F.R. § 76.906.

[11] 47 C.F.R. § 76.911(b)(1).

[12] *Third Recon. Order, supra.*

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Star Cable challenging the certification of Floyd County to regulate basic cable rates IS GRANTED.

6. IT IS FURTHER ORDERED that the certification of Floyd County to regulate Star Cable's basic cable rates IS RESCINDED.

7. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

AMERICAN CABLE COMPANY

Petition for Reconsideration
of the Certification of
City of Columbus, Georgia
to Regulate Basic Cable Rates
(GA0753)

MEMORANDUM OPINION AND ORDER

Adopted: November 22, 1994; Released: November 23, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On May 10, 1994, American Cable Company ("American") filed a petition for revocation challenging the certification of the City of Columbus, Georgia (the "City") to regulate rates for basic cable service and associated equipment.[1] In its petition, American also requested that a stay of rate regulation be granted pending the resolution of the petition. The City filed an objection to American's petition. On August 12, 1994, American submitted a supplement providing documentation in support of its petition pursuant to a recent Commission order.[2]

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[3] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[4] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[5] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[6] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[7] After the 30-day deadline for filing petitions for reconsideration has elapsed, cable operators may challenge the franchising authority's certification by filing a petition for revocation.[8] However, regardless of its grounds, a petition for revocation does not automatically trigger a stay of the franchising authority's power to regulate basic rates.[9]

II. DISCUSSION

3. American argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in the City, the franchise area.[10] The supplement to American's petition shows that the cable system currently serves 4,799 of the 65,942 households in the franchise area, or 7.3 percent of the total number of households. As supporting documentation, American provides 1990 Census data[11] which shows that there are 65,942 households (that is, occupied housing units)[12] in the franchise area. American also submits a computer print-out with sufficient subscriber information to show that it serves 4,799 households in the franchise area. Finally, American provides affidavits by a responsible official certifying the accuracy of the data included in the petition and the supplement to the petition.

4. The City concedes that American serves fewer than 30 percent of the households in the franchise area. The City's objection to American's petition is based on its contention that American has made an affirmative decision to limit its actual service area.[13] The City claims that American has not satisfied certain "must build provisions" of the franchise agreement requiring American to establish a particu-

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[1] The City filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on September 28, 1993, which became effective on October 28, 1993.

[2] *Cable Operators' Petition for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994).

[3] 47 U.S.C. § 543(a)(4).

[4] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[5] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition.47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[6] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[7] 47 C.F.R. § 76.911(c).

[8] 47 C.F.R. § 76.914.

[9] 47 C.F.R. § 76.914(d).

[10] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[11] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994).

[12] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*"Third Recon. Order"*). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[13] In the *First Order on Reconsideration*, the Commission

lar service area by January 1, 1990 and eventually serve the entire franchise area where population density exceeds 35 occupied dwellings per mile. The City claims that, as a result, American has redefined the franchise area for purposes of the effective competition standard. In response, American refers the Commission to its pleadings in two other proceedings (Nos. CSR 4206 and CSR 4198-P) in which it claims that its competitor, by engaging in discriminatory pricing and unfair methods of competition, has prevented it from expanding its service area in the City.

5. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[14] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[15] American has met this burden.

6. As a preliminary matter, we are unpersuaded that the appropriate franchise area for purposes of effective competition is something less than the entire City of Columbus. The City provides insufficient evidence to support its claim that American has made an affirmative decision to limit its service to the more densely populated areas within the City. Without providing adequate support for its claims, the City merely concludes that American has decided not to serve the entire franchise area since certain service requirements of the franchise agreement have not been met. However, "[t]he fact that a franchise area has not as yet been filled out by construction of a system would not by itself be taken as redefining the service area.[16] Therefore, we find that the City has failed to sustain its burden of proof that American has redefined its franchise area.

7. American appropriately relied on data reflecting the number of households as required by our rules.[17] Relying on this data, American has submitted sufficient evidence demonstrating that its cable system serving the City, its franchise area, serves 4,799 of the 65,942 households, or 7.3 percent of the households, within its franchise area. Thus, we find American's system serving the City of Columbus is subject to effective competition. Accordingly, its petition is granted.

III. ORDERING CLAUSES

8. Accordingly, IT IS ORDERED that the petition for revocation filed by American Cable Company challenging the certification of the City of Columbus IS GRANTED.

9. IT IS FURTHER ORDERED that the certification of the City of Columbus, Georgia to regulate American's basic cable rates IS RESCINDED.

10. IT IS FURTHER ORDERED that American's request for a stay of rate regulation IS DISMISSED as moot.

11. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

clarified the definition of "franchise area" for purposes of determining effective competition. *First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking,* MM Docket No. 92-266, 9 FCC Rcd 1164 (1993) (*"First Recon. Order"*). Generally, "[a] franchise area is the area a system operator is granted authority to serve in its franchise." *Id.* at 1180. The Commission stated, however, that a more restricted definition of "franchise area" may be appropriate under limited circumstances, such as when an operator "has itself, through its own conduct, self-defined the areas to be served to such an extent that this redefined area accurately portrays the operator's 'franchise area.'" *Id.* at 1181. Under this standard, the franchising authority has the burden of showing that the operator has made an affirmative decision . . . to restrict service." *Id.*

[14] 47 C.F.R. § 76.906.

[15] 47 C.F.R. § 76.911(b)(1).

[16] *First Recon. Order, supra.*

[17] *Third Recon. Order, supra.*

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

STAR CABLE ASSOCIATES

Petition for Reconsideration
of the Certification of
Leroy Township, Ohio
to regulate basic cable rates
(OH2064)

MEMORANDUM OPINION AND ORDER

Adopted: November 22, 1994; Released: November 23, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On November 18, 1993, Star Cable Associates ("Star Cable") filed a timely petition for reconsideration challenging the certification of Leroy Township, Ohio to regulate rates for basic cable service and associated equipment.[1] Leroy Township did not file an opposition to Star Cable's petition.

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[2] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[3] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[4] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[5] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[6]

II. DISCUSSION

3. Star Cable argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in Leroy Township, its franchise area.[7] Star Cable claims that it currently serves only 43 of the 851 households (that is, occupied housing units)[8] in Leroy Township, or 5.1 percent of the total number of households. As supporting documentation, Star Cable provides 1990 Census data[9] which shows that there are 851 households in Leroy Township. Star Cable also submits a computer print-out with sufficient subscriber information to support its claim that it serves 43 subscribers in the franchise area. Finally, Star Cable provides an affidavit by a responsible official certifying the accuracy of the data included in the petition.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[10] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[11] Star Cable has met this burden. Star Cable appropriately relied on data reflecting the number of households as required by our rules.[12] Relying on this data, Star Cable has submitted sufficient evidence demonstrating that its cable system serving Leroy Township, its franchise area, serves 43 of the 851 households, or 5.1 percent of the households, within its franchise area. Thus, we find Star Cable's system serving Leroy Township is subject to effective competition. Accordingly, its petition is granted.

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Star Cable challenging the certification of Leroy Township to regulate basic cable rates IS GRANTED.

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[1] Leroy Township filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on September 27, 1993, which became effective on October 27, 1993.

[2] 47 U.S.C. § 543(a)(4).

[3] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[4] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition. 47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[5] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[6] 47 C.F.R. § 76.911(c).

[7] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[8] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*"Third Recon. Order"*). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[9] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994).

[10] 47 C.F.R. § 76.906.

[11] 47 C.F.R. § 76.911(b)(1).

[12] *Third Recon. Order, supra.*

6. IT IS FURTHER ORDERED that the certification of Leroy Township to regulate Star Cable's basic cable rates IS RESCINDED.

7. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

COMMUNICATION TELESYSTEMS INTERNATIONAL — File No. I-T-C-94-475

Application for authority to acquire and operate facilities between the United States mainland and Puerto Rico.

ORDER, AUTHORIZATION AND CERTIFICATE

Adopted: November 21, 1994; Released: December 5, 1994

By the Chief, Telecommunications Division:

1. Upon consideration of the above-captioned uncontested application, filed pursuant to Section 214 of the Communications Act of 1934, as amended, IT IS HEREBY CERTIFIED that the present and future public convenience and necessity require a grant thereof.

2. Accordingly, IT IS ORDERED that application File No. I-T-C-94-475 IS GRANTED, and Communication Telesystems International (CTS) is authorized to:

a. acquire on an original ownership basis and operate one 2.048 Mbps circuit in the Americas-1 Cable System between Florida and St. Thomas, U.S. Virgin Islands;

b. acquire on an Indefeasible Right of User (IRU) basis one 2.048 Mbps circuit in the Taino-Caribe Cable System between St. Thomas and Puerto Rico;

c. lease and operate necessary connecting facilities in the United States and Puerto Rico; and

d. use said facilities to provide CTS' regularly authorized services, including switched voice and data and private line services, between the United States and Puerto Rico, and between the United States and international points CTS is authorized to serve.[1]

3. IT IS FURTHER ORDERED that neither CTS nor any persons or companies directly or indirectly controlling or controlled by CTS, or under direct or indirect common control with it, shall acquire or enjoy any right, for the purposes of handling or interchanging traffic to or from the United States, its territories or possessions, which is denied to any other United States carrier by reason of any concession, contract, understanding, or working arrangement to which CTS or any persons or companies controlling or controlled by CTS are parties.

4. IT IS FURTHER ORDERED that our authorization of CTS to provide private lines as part of its authorized services is limited to the provision of such private lines only between the United States and the countries CTS is authorized to serve -- that is, private lines which originate in the United States and terminate in one of the countries served by CTS or which originate in one of the countries served by CTS and terminate in the United States. In addition, CTS may not -- and CTS's tariff must state that its customers may not -- connect private lines provided over these facilities to the public switched network at either the U.S. or foreign end, or both, for the provision of international basic telecommunications services, including switched voice services, unless authorized to do so by the Commission upon a finding that the destination country affords resale opportunities equivalent to those available under U.S. law, in accordance with *Regulation of International Accounting Rates, Phase II, First Report and Order*, 7 FCC Rcd 559 (1991), Order on Reconsideration and Third Further Notice of Proposed Rulemaking, 7 FCC Rcd 7927 (1994), *petition for reconsideration pending.*

5. IT IS FURTHER ORDERED that the applicant shall file copies of any operating agreements entered into with its foreign correspondents with the Commission within 30 days of their execution, and shall otherwise comply with the filing requirements contained in Section 43.51 of the Commission's Rules, 47 C.F.R. §43.51.

6. IT IS FURTHER ORDERED that the applicant shall file a tariff pursuant to Section 203 of the Communications Act, 47 U.S.C. §203 and Part 61 of the Commission's Rules, 47 C.F.R. Part 61, for the services authorized in this Order.

7. IT IS FURTHER ORDERED that the applicant shall file the annual reports of overseas telecommunications traffic required by Section 43.61 of the Commission's Rules, 47 C.F.R. §43.61.

8. IT IS FURTHER ORDERED that the applicant shall file semi-annual circuit reports pursuant to Section 63.15(b) of the Commission's Rules, 47 C.F.R. §63.15(b), for the common carrier facilities authorized herein.

9. This Order is issued under Section 0.261 of the Commission's Rules and is effective upon adoption. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the date of public notice of this Order (see Section 1.4(b)(2)).

FEDERAL COMMUNICATIONS COMMISSION

Diane J. Cornell
Chief, Telecommunications Division
International Bureau

[1] *Communication Telesystems International*, DA-94-617, File No. I-T-C-94-217, released June 20, 1994.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Amendment of Part 90 of the Commission's Rules to Facilitate Future Development of SMR Systems in the 800 MHz Frequency Band	**PR Docket No. 93-144** RM-8117, RM-8030 RM-8029
and	
Implementation of Section 309(j) of the Communications Act - Competitive Bidding 800 MHz SMR	**PP Docket No. 93-253**

ORDER

Adopted: November 28, 1994; Released: November 28, 1994

By the Acting Chief, Land Mobile and Microwave Division:

1. We have received requests from the American Mobile Telecommunications Association, Inc. ("AMTA") and SMR WON for an extension of time for filing Comments and Reply Comments in response to the *Further Notice of Proposed Rule Making* in this proceeding.[1] AMTA's motion, filed on November 22, 1994, requests that the Commission extend the deadlines for filing comments and reply comments (currently December 5, 1994 and December 20, 1994, respectively) by 30 days. SMR WON's motion, filed on November 21, 1994, requests that the deadlines be extended by 60 days. To date, no opposition to either request has been filed.

2. AMTA seeks a 30-day extension so that it may work with its members, who represent a broad cross-section of small and large Specialized Mobile Radio (SMR) providers, to achieve consensus regarding the numerous and complex issues raised by the *Further Notice*. AMTA observes that the proposals presented in the *Further Notice* would have "significant, yet different, implications for those intending to provide wide-area services versus those who plan to maintain their systems in a more traditional configuration."[2] As a result, AMTA contends that it is imperative that the SMR industry be given sufficient time not only to evaluate the proposals fully but also to seek a consensus on as many issues as possible.

3. SMR WON, a new organization representing SMR operators in smaller markets and rural areas, states that a 60-day extension is needed so that its consultants may prepare economic and engineering studies that it intends to rely on in filing comments. SMR WON also contends that additional time is necessary to achieve industry consensus given the current disagreements among members of the industry about issues raised in this proceeding.

4. We agree with both AMTA and SMR WON that the public interest would be served by granting an extension so that members of the SMR industry have the opportunity to reach consensus about the proposals presented in this proceeding. Both parties indicate that discussions among industry members are under way, but that the current comment deadlines do not allow sufficient time for consensus positions to develop. We therefore agree with AMTA that a 30-day extension of the comment period is appropriate. We emphasize that in granting this extension, we expect SMR industry representatives to use the additional time productively to seek a consensus on as many issues as possible and to ensure that the Commission receives thorough and well-reasoned comments on all issues in this proceeding.

5. We also decline to grant SMR WON's request for a 60-day extension. SMR WON asserts that a 60-day extension is necessary to enable its economic and engineering consultants to complete studies that SMR WON has commissioned for this proceeding. SMR WON's motion indicates, however, that these consultants were not retained until after November 4, 1994.[3] We note that hiring of consultants is a matter within SMR WON's control and could have occurred at an earlier date. We also reject SMR WON's contention that the Commission did not provide sufficient detail regarding its proposals prior to November 4, when the *Further Notice* text was released, to enable SMR WON to commence its analysis earlier. In fact, the Commission outlined the major details of its 800 MHz SMR proposal well before November in the *Third Report and Order* in GN Docket No. 93-252.[4]

6. Accordingly, IT IS HEREBY ORDERED that the Motion of Extension of Time filed by the American Mobile Telecommunications Association is GRANTED, and the Motion for Extension of Time filed by SMR WON is hereby DENIED.

7. IT IS FURTHER ORDERED, pursuant to Section 1.46 of the Commission's Rules, 47 C.F.R. § 1.46, that the deadline for filing initial comments in this proceeding is extended from December 5, 1994 to January 5, 1995, and that the deadline for filing reply comments is extended from December 20, 1994 to January 20, 1995.

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[1] *Further Notice of Proposed Rule Making*, Amendment of Part 90 of the Commission's Rules to Facilitate Future Development of SMR Systems in the 800 MHz Frequency Band and Implementation of Section 309(j) of the Communications Act - Competitive Bidding, 800 MHz SMR, PR Docket No. 93-144 and PP Docket No. 93-253, FCC 94-271, adopted October 20, 1994, released November 4, 1994 (*Further Notice*).

[2] AMTA Motion at 3.

[3] *See* SMR WON Motion at 2, 3.

[4] *See Third Report and Order*, Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services, GN Docket No. 93-252, FCC 94-212, adopted August 9, 1994, released September 23, 1994, at paras. 95-106.

FEDERAL COMMUNICATIONS COMMISSION

Rosalind K. Allen
Acting Chief, Land Mobile and Microwave Division
Private Radio Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

PUBLIC NOTICE

Released: November 29,1994

STATUS OF THE
BOCS' JOINT CONTINGENCY PETITION
FOR INTERIM WAIVER OF THE
COMPUTER II RULES
UNDER THE COMMISSION'S EX PARTE RULES

On November 14, 1994, Ameritech Operating Companies, Bell Atlantic Telephone Companies, BellSouth Telecommunications Inc., NYNEX Telephone Companies, Pacific Bell and Nevada Bell, Southwestern Bell Telephone Company, US West, Inc, and US West Communications, Inc. (BOCs) filed a joint contingency petition for an interim waiver of the Commission's *Computer II* rules. The BOCs state that they are requesting a waiver, to the extent it is necessary, to enable them to continue offering enhanced services on an integrated basis to approximately five million BOC customers without service disruption. The BOCs state that they filed the petition in light of the recent Court of Appeals decision for the Ninth Circuit. (*People of the State of California v. FCC*, Slip Opin., Oct. 18, 1994, *California III)*.

We will treat this proceeding as non-restricted for purposes of the Commission's *ex parte* rules. *See generally* 47 C.F.R. §§ 1.1200-1.1216. Any party that has made an *ex parte* presentation prior to the issuance of this Public Notice should submit a written summary of that presentation in accordance with 47 C.F.R. §1.1206.

FEDERAL COMMUNICATIONS COMMISSION

Before the
Federal Communications Commission
Washington, D.C. 20554

PUBLIC NOTICE

Released: November 28, 1994

PLEADING CYCLE ESTABLISHED FOR COMMENTS ON PACIFIC BELL'S PETITION FOR AN INTERIM WAIVER OF THE COMMISSION'S RULES TO OFFER ISDN EQUIPPED ACCESS LINES WITHOUT IMPOSITION OF THE END USER COMMON LINE CHARGE

On November 9, 1994, Pacific Bell (Pacific) petitioned the Commission for an interim waiver of Section 69.104 of the Commission's rules to provide ISDN equipped access lines to schools, libraries, and community colleges without an associated End User Common Line (EUCL) charge. Pacific states that it has initiated a program called "Education First," whereby it will provide public and private K-12 schools, public libraries, and community colleges with ISDN lines. Pacific proposes to provide up to four ISDN lines per eligible institution without cost for the first year, and seeks a waiver of the EUCL normally assessed on these lines for one year.

Pacific estimates that the cost of the program will be up to approximately $115 million, and that the costs will be split fairly evenly between expenses and foregone revenue. Pacific estimates that the foregone revenue from EUCL could be as much as an additional $2.3 million, spread over the three-year period that this program will be in effect. Pacific states that this cost will be borne by shareholders, not ratepayers. Pacific states the waiver would be in the public interest by accelerating technological advancements in schools and libraries. Pacific states that it has already received permission from the California Public Utilities Commission to offer this program.

Interested parties may file comments on this petition for interim waiver **December 8, 1994,** and reply comments by **December 15, 1994,** with the Secretary, FCC, 1919 M Street, N.W., Washington, D.C. 20554. A copy should also be sent to Peggy Reitzel, Common Carrier Bureau, FCC, Room 544, 1919 M Street, N.W., Washington, D.C. 20554, and to the Commission's contractor for public service records duplication: ITS, Inc., 2100 M Street, N.W., Suite 140, Washington, D.C. 20037. Copies of the petition for waiver can be obtained from ITS, Inc. at (202) 857-3800.

We will treat this proceeding as non-restricted for purposes of the Commission's *ex parte* rules. *See generally,* 47 C.F.R. §§1.1200-1.1216. For further information contact Peggy Reitzel, Policy and Program Planning Division of the Common Carrier Bureau, at (202) 418-1579.

FEDERAL COMMUNICATIONS COMMISSION

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Southwestern Bell Telephone Company
Request for Waiver of Tandem Signalling
Interconnection Requirementshh,

ORDER

Adopted: November 23, 1994; Released: November 28, 1994

By the Chief, Common Carrier Bureau:

I. INTRODUCTION

1. In order to further promote competition in the interstate access marketplace, 0the Commission issued a *Third Report and Order* on May 27, 1994 requiring Tier 1 local exchange carriers (LECs) to provide the signalling information necessary for competitors to provide tandem switching in competition with the LECs.[1] The *Third Report and Order* directed the LECs to file tariffs implementing its requirements no later than September 26, 1994, effective on 45 days' notice on November 10, 1994. On September 20, 1994, Southwestern Bell Telephone Company (Southwestern Bell) filed a Request for Waiver (Waiver Request) of certain requirements of the *Third Report and Order*. For the reasons discussed below, we deny the Waiver Request.

II. BACKGROUND

2. The *Third Report and Order* continued the Commission's efforts to remove barriers to competition in interstate access services. The order required LECs to make available to all interested parties, including competitive access providers (CAPs), interexchange carriers (IXCs), and end users, the signalling information necessary to provide tandem switching functions for switched transport services. Those third parties, known as Tandem Switching Providers (TSPs), would then be able to interconnect their own tandems with LEC equal access end offices and compete with LECs in providing tandem switched transport. The Commission concluded that the benefits of such competition, in the form of reduced rates, stimulation of investment, and increased network redundancy, far outweighed the relatively slight cost to LECs of making signalling information available.[2]

3. The *Third Report and Order* required all Tier 1 LECs, other than National Exchange Carrier Association (NECA) pool members, to transmit Carrier Identification Codes (CIC) (specifying the IXC to handle the call) and OZZ codes (identifying the IXC trunk group to carry the call) to interconnected TSP tandems.[3] The Commission concluded that any necessary technical and billing changes could be made without significant expense or delay, and directed LECs to file tariffs consistent with the *Third Report and Order* no later than September 26, 1994, with an effective date of November 10, 1994.[4] All of the LECs subsequently filed tariffs by September 26, 1994, and the Tariff Division, as part of the tariff review process, deferred the tariff effective date for 120 days, until January 21, 1995 for BellSouth and January 24, 1995 for all other LECs.

III. POSITIONS OF THE PARTIES

A. Southwestern Bell's Waiver Request

4. Southwestern Bell claims that several of the requirements of the *Third Report and Order* are either unreasonable, technically infeasible, or would require up to 24 additional months for switch modifications and industry-wide consultation.[5] First, Southwestern Bell requests that it not be required to use TSP-provided billing tapes to bill IXCs for terminating traffic routed through TSP tandems.[6] According to Southwestern Bell, LECs must depend on TSP billing tapes because LEC end offices cannot identify the amount to bill an IXC when the IXC is the customer of record for terminating traffic routed through TSP tandems. Southwestern Bell claims that this requirement places LECs "at the mercy of their competitors," and that TSPs may not provide necessary billing recordings

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[1] *Expanded Interconnection with Local Telephone Company Facilities*, CC Docket No. 91-141, Transport Phase II, *Third Report and Order*, 9 FCC Rcd 2718 (1994) (*Third Report and Order)*. The *Third Report and Order* built upon two previous orders requiring LECs to provide expanded interconnection for interstate special access and for switched transport services. *Expanded Interconnection with Local Telephone Company Facilities*, Report and Order and Notice of Proposed Rulemaking, 7 FCC Rcd 7369 (1992) (*Special Access Interconnection Order), recon.*, 8 FCC Rcd 127 (1992), *further recon.*, 8 FCC Rcd 7341 (1993), *vacated in part and remanded sub nom. Bell Atlantic Telephone Cos. v. FCC*, 24 F.3d 1441 (D.C. Cir. 1994); *Expanded Interconnection with Local Telephone Company Facilities*, Second Report and Order and Third Notice of Proposed Rulemaking, 8 FCC Rcd 7374 (1993) (*Switched Transport Expanded Interconnection Order), pet. for review pending sub nom. Bell Atlantic v. FCC*, No. 93-1743 (D.C. Cir., filed Nov. 12, 1993); *see also Expanded Interconnection with Local Telephone Company Facilities*, Memorandum Opinion and Order, FCC 94-190, 9 FCC Rcd 5154 (1994), *appeal docketed sub nom.* Southwestern Bell Telephone Co. v. FCC, No. 94-1547 (D.C. Cir. Aug. 10, 1994).

[2] *Third Report and Order*, 9 FCC Rcd at 2724-25, ¶ ¶ 25-26.

[3] *Id.* at 2721, 2724, ¶ ¶ 14, 24.

[4] *Id.* at 2730, ¶ 57.

[5] Prior to filing the waiver request that is the subject of this order, Southwestern Bell made many of the same arguments in a Petition for Clarification and Reconsideration of the *Third Report and Order. Petition for Clarification and Reconsideration of Southwestern Bell Telephone Company* (July 27, 1994). Action on Southwestern Bell's reconsideration petition is currently pending. Southwestern Bell also claimed in its comments responding to the Notice of Proposed Rulemaking that led to the *Third Report and Order* that the provision of tandem signalling information would cause general technical difficulties, but it did not describe the specific problems it asserts here. *See* Comments of Southwestern Bell Telephone Company on Third Notice of Proposed Rulemaking, CC Docket No. 91-141, Transport Phase II (April 5, 1993) at 20.

[6] Waiver Request at 2.

promptly or in an acceptable format.[7] As an alternative, Southwestern Bell proposes that TSPs be required to be the terminating customers of record and to maintain separate terminating trunk groups.[8]

5. Southwestern Bell further requests that it only be required to provide signalling information to TSPs in a multi-frequency (MF) environment, rather than in a common channel Signalling System 7 (SS7) environment.[9] Southwestern Bell asserts that in order for it to recognize and pass the necessary signalling information to TSPs, its network must treat TSP tandems as similar to its own tandems. Southwestern Bell contends that although this would give TSPs the information they need to provide competitive tandem switched transport, it would not permit Southwestern Bell to distinguish and bill accurately calls directed to TSP tandems, leading to overbilling of TSPs.[10] According to Southwestern Bell, the only feasible method of addressing this problem requires the use of standardized Trunk Group Numbers for calls routed through interconnected TSP tandems.[11] Trunk Group Numbers would identify the specific trunks that calls are directed through, providing the necessary routing information in the network billing record to determine whether calls have been sent to a LEC or a TSP tandem. Industry-wide numbering standards for Trunk Group Numbers do not exist, however. Southwestern Bell asserts that, in an SS7 environment, it must rely on Trunk Group Numbers assigned by TSPs, and that "it would only be by chance" that the TSP would assign a Trunk Group Number that would allow Southwestern Bell to properly bill the call.[12] Southwestern Bell states that, as LECs control the assignment of Trunk Group Numbers in an MF signalling environment, such additional efforts would not be necessary if SS7 signalling were not used. According to Southwestern Bell, development of protocols to ensure that Trunk Group Numbers assigned by Southwestern Bell and TSPs do not conflict would require extensive consultation in industry fora, and might necessitate costly and time-consuming network modifications.[13]

6. Southwestern Bell also asks that it not be required to permit overflow from LEC tandems to TSP tandems, or vice versa.[14] Southwestern Bell claims that if an IXC designated a TSP tandem for primary traffic and a LEC tandem for overflow traffic, or vice versa, Southwestern Bell would be unable to identify and bill overflow calls properly, because its billing recording would still identify overflow calls as passing through the primary tandem.[15] Difficulties in billing overflow calls could also be addressed through the use of standardized Trunk Group Numbers, but, according to Southwestern Bell, the absence of industry-wide Trunk Group Number standards prevents timely adoption of this solution here as well.[16]

7. Finally, Southwestern Bell states that the existing tariff filing schedule provides insufficient time for it to resolve various other billing issues both internally and in consultation with interested parties.[17] Southwestern Bell therefore asks that the Commission defer the tariff filing date to December 30, 1994, and the implementation date to March 1, 1995.

B. Pleadings

8. The Association for Local Telecommunications Services (ALTS), AT&T Corp. (AT&T), MCI Telecommunications Corp. (MCI), and WilTel, Inc. (WilTel) filed comments on the Waiver Request. All of these parties oppose the substantive waivers sought by Southwestern Bell, although MCI and WilTel do not object to Southwestern Bell's request for an extension of the tariff filing and effective dates.

9. With regard to TSP-provided billing recordings, ALTS characterizes Southwestern Bell's concerns as "frivolous,"[18] and argues that carriers in the telecommunications industry and in other utilities have used one another's records for proper billing for many years. JALTS further claims that other LECs have not found it necessary to request such a waiver, and I that any problems involving shared billing records can be resolved through consultations between Southwestern Bell and TSPs.[19] WilTel argues that the Commission has already considered and rejected Southwestern Bell's concerns about utilizing TSP-provided billing recordings.[20]

10. Commenters also oppose Southwestern Bell's request that it only be required to provide MF, and not SS7, signalling. ALTS notes that no other LEC has asserted similar problems in providing SS7 signalling interconnection, and that difficulties involving nonstandardized Trunk Group Numbers could be resolved by requiring a TSP to agree to a LEC's Trunk Group Number numbering conventions as a condition of providing interconnection.[21] AT&T claims that the conditions Southwestern Bell proposes to impose would degrade the quality of access available to TSPs and would unreasonably increase costs, when more reasonable alternatives are available.[22] MCI contends that Southwestern Bell's request that SS7 signalling issues be referred to industry fora is a "ruse" designed to delay indefinitely the implementation of competitive tandem

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[7] *Id.* at 2-3.

[8] *Id.* at 3.

[9] *Id.* at 4. In an MF signalling environment, call setup and billing information is transmitted through the same circuits as the call itself. In a common channel signalling SS7 environment, call setup and billing data are transmitted through separate network facilities from those that transmit the actual communications between the calling party and the called party, allowing for much faster call setup times and facilitating advanced features.

[10] *Id.* at 4-5. Southwestern Bell claims that, if TSP tandems are treated by its network as its own tandems, TSPs (or the customers of record if not the TSP) would be billed for tandem switching and tandem switched transport, just as if the call had been routed through Southwestern Bell's tandem, even though the call would not be using the Southwestern Bell tandem.

[11] *Id.* at 5. Southwestern Bell states that Trunk Group Numbers provide the necessary information in its network billing recordings to determine whether individual calls were directed to its own tandems or to a TSP's tandems. Neither Southwestern Bell nor any of the commenters offer further details about how Trunk Group Numbers address the problems Southwestern Bell raises, although no party contests Southwestern Bell's claim that the use of standardized Trunk Group Numbers would be an effective solution.

[12] *Id.*

[13] *Id.* at 5-6.

[14] *Id.* at 6.

[15] *Id.* at 6-7.

[16] *Id.*

[17] *Id.* at 7.

[18] ALTS Comments at 1.

[19] *Id.* at 2-3.

[20] WilTel Comments at 2.

[21] ALTS Comments at 4.

[22] AT&T Comments at 3.

switching,[23] and that MCI has requested certain of these SS7 capabilities from Southwestern Bell since 1987.[24] WilTel states that, by Southwestern Bell's own admission, the development of industry standards for Trunk Group Numbers will resolve the SS7 signalling problem.[25] According to WilTel, a limited extension of time to allow for Trunk Group Number standardization, rather than a waiver of the SS7 signalling requirement, would best address the concerns Southwestern Bell raises.

11. Similarly, commenters reject Southwestern Bell's arguments in support of its claim that it should not be required to allow overflow between LEC and TSP tandems. ALTS claims that the amount of overflow traffic will initially be minimal, and that the estimated cost of such traffic can be billed up front to customers who request overflow to LEC tandems.[26] WilTel argues that overflow between LEC and TSP tandems is unlikely ever to occur unless the Commission modifies the *Third Report and Order* to require LECs to offer signalling from their tandems as well as from their end offices.[27] Even if overflow were to occur, WilTel claims, Trunk Group Number standardization would solve the problems Southwestern Bell describes.[28]

12. Commenters are split on Southwestern Bell's request that the tariff filing date be deferred to December 30, 1994. MCI states that it supports a three-month delay in tariff filing and effective dates, but urges the Commission to reject any further delays in implementation of the *Third Report and Order*.[29] WilTel does not object to a delay in tariff filing requirements of up to six months.[30] By contrast, ALTS claims that Southwestern Bell has not raised any legitimate billing issues that would necessitate a delay in tariff filing dates.[31]

13. In reply, Southwestern Bell dismisses claims by other parties that the problems it identifies could be solved at little cost and in a short period of time as "unrealistic."[32] With regard to TSP-provided billing tapes, Southwestern Bell contends that it is aware of no other situation in which a company is forced to bill its own charges based solely on information provided by competitors who have clear incentives to understate such charges.[33] Southwestern Bell asserts that "[h]istory has proven" that the time frame it suggests for resolving Trunk Group Number standardization issues is reasonable.[34] As for overflow, Southwestern Bell wasserts that LECs currently provide for overflow from a direct route to a tandem route, but that overflow between two tandems presents a substantially different situation.[35] Finally, Southwestern Bell notes that no party makes any strenuous objections to a short delay in tariff filing and effective dates.[36]

IV. DISCUSSION

14. The Commission may waive any provision of its rules or orders on petition if good cause is shown.[37] A showing of good cause requires the petitioner to demonstrate special circumstances that warrant deviation from the rule and to show how such deviation would serve the public interest.[38] Reconsideration of the *Third Report and Order* is currently pending; in this order we address only the question of whether Southwestern Bell has shown good cause for waiver of any of the requirements of the *Third Report and Order*. We conclude that a waiver of those requirements would not serve the public interest, and deny Southwestern Bell's Waiver Request.

A. Use of TSP Billing Recordings

15. We decline to waive our requirement that LECs accept TSP billing tapes to bill terminating traffic. The Commission specifically addressed this issue in the *Third Report and Order*, and rejected claims by LECs that problems would arise if they were required to use TSP-provided billing tapes.[39] Southwestern Bell raises no new arguments in its Waiver Request that would justify deviation from our previous decision.[40] Nor does Southwestern Bell present any special circumstances that would justify a waiver. The *Third Report and Order* obligates TSPs to provide the necessary billing tapes to LECs, and Southwestern Bell may negotiate any "fair and reasonable procedures" it feels are necessary to resolve billing disputes.[41] As commenters have pointed out in response to Southwestern Bell's Waiver Request, the exchange of billing information among different carriers is not uncommon in the telecommunications industry or in other regulated utility industries.[42] Southwestern Bell's proposed alternatives – that TSPs be required to be the terminating customers of record and to construct separate terminating trunk groups to LEC end offices – would make it less economical for TSPs to provide competitive tandem switched transport. That result would undermine achievement of the primary objective of the *Third Report and Order:* to foster competition in interstate access services.

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23 MCI Comments at 4.
24 *Id.*
25 WilTel Comments at 2-3.
26 ALTS Comments at 4.
27 WilTel Comments at 3.
28 *Id.*:
29 MCI Comments at 4-5.
30 WilTel Comments at 1.
31 ALTS Comments at 5. ALTS asserts that the only billing issue raised by Southwestern Bell other than the SS7 and overflow issues discussed above involves Southwestern Bell's desire to bill tandem signalling on a usage-sensitive basis. ALTS argues that such usage-sensitive charges would be "a bad idea" because charges, especially initially, would be "infinitesimal." *Id.* at 5-6.
32 Southwestern Bell Reply at 4-5.
33 *Id.* at 3.
34 *Id.* at 2.
35 *Id.* at 5.
36 *Id.* at 5.
37 47 C.F.R. § 1.3.
38 Northeast Cellular Telephone Co. v. FCC, 897 F.2d 1164, 1166 (D.C. Cir. 1990).
39 *Third Report and Order*, 9 FCC Rcd at 2725, ¶ 31.
40 "The very essence of a waiver is the assumed validity of the general rule . . . ." *WAIT Radio v. FCC*, 418 F.2d 1135, 1158 (D.C. Cir. 1969), *cert. denied*, 409 U.S. 1027 (1972).
41 *Third Report and Order*, 9 FCC Rcd at 2725, ¶ 31.
42 ALTS Comments at 2.

B. Provision of SS7 Signalling

16. We decline to waive the requirement of the *Third Report and Order* that, at the option of the TSP, LECs provide SS7 signalling information in end offices in which common channel signalling is available. Southwestern Bell has not explained why waiver of this requirement would serve the public interest. Indeed, even Southwestern Bell recognizes that its concerns about distinguishing LEC and TSP tandems in an SS7 environment can be addressed through the use of Trunk Group Numbers. We are not persuaded by Southwestern Bell's assertions that resolution of Trunk Group Number standardization issues will require extensive industry-wide consultation and up to 24 months and millions of dollars for network modifications. We note that all of the other LECs filing tariffs to provide tandem switch interconnection have agreed to provide SS7 signalling.[43] Although Southwestern Bell's network may be less technically capable than other LECs' networks, Southwestern Bell has not identified any specific limitations that would justify a waiver. Given the benefits of SS7 signalling, such as faster call setup times, we believe that a waiver of the SS7 signalling requirement would reduce the likelihood of effective competition in tandem switched transport, and therefore would not be in the public interest. We recognize that some discussion of Trunk Group Number standardization may need to occur within the industry or between individual LECs and TSPs. The Tariff Division has already deferred the effective date of all LEC tandem signalling tariffs until January 21, 1995 or January 24, 1995.[44] We believe that this delay should be sufficient, assuming good faith efforts by all parties, to resolve any difficulties in providing SS7 signalling information.

C. Overflow Between LEC and TSP Tandems

17. The *Third Report and Order* contemplated that IXCs would be able to designate a primary route and an "overflow" route, which would be used if there was insufficient capacity on the primary route, for their traffic.[45] Southwestern Bell does not suggest in its Waiver Request that it would be unable to provide for overflow from IXC direct trunks to a TSP's tandems. Indeed, Southwestern Bell concedes in its reply that it can provide for such overflow from a direct route.[46] Southwestern Bell, however, interprets the *Third Report and Order* as mandating that it allow overflow not only from direct routes, but also between its own and a TSP's tandem, and asks for a waiver of that requirement.

18. Southwestern Bell has misinterpreted the Commission's decision. The *Third Report and Order* does not require tandem-to-tandem overflow. In fact, the Commission stated that "[t]he record fails to indicate . . . that any entity would actually seek to offer or use that kind of routing dynamic."[47] As the requirement from which Southwestern Bell seeks relief does not exist, we need not grant Southwestern Bell a waiver of such a requirement.

D. Extension of Time

19. Southwestern Bell has failed to show that any of the substantive difficulties it describes are serious enough to justify a waiver of the requirements of the *Third Report and Order*. Although Southwestern Bell asserts that it will be unable to make necessary billing modifications before March 1, 1995, it has not identified any specific problems or special circumstances that might support an extension of tariff filing and effective dates, other than those we have addressed above. We do not believe that unnecessary delay in the emergence of competition in tandem switched transport would serve the public interest. Southwestern Bell's requested extension of the tariff filing date until December 30, 1994, with an effective date of March 1, 1995 and the possibility of additional delays in the tariff review process, would allow for an unreasonable divergence from the timetable established in the *Third Report and Order*. We therefore deny Southwestern Bell's request that the tariff filing date requirement of the *Third Report and Order* be waived.

20. As we have noted, however, the Tariff Division has deferred the effective date of all the LECs' tariffs for the statutory maximum 120 days.[48] Consequently, Southwestern Bell's tariff will not become effective until January 24, 1995. We believe that this additional time will provide the LECs and other parties a further opportunity to work together to solve the implementation problems relating to the provision of tandem signalling information. We encourage Southwestern Bell and other LECs to use of this extension to address the Trunk Group Number standardization issue Southwestern Bell raises in its Waiver Request, and to complete any necessary billing modifications.

V. CONCLUSION

21. Southwestern Bell has not convinced us that good cause exists to waive any of the requirements of the *Third Report and Order*. We therefore deny Southwestern Bell's Waiver Request.

VI. ORDERING CLAUSE

22. Accordingly, it is ORDERED, pursuant to authority contained in Sections 1, 4, and 201-205 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, and 201-205, and Sections 0.91, 0.201-0.204, and 0.291 of the Commission's Rules, 47 C.F.R. §§ 0.91, 0.201-0.204, and 0.291, that Southwestern Bell Telephone Company's Request for Waiver IS DENIED.

FEDERAL COMMUNICATIONS COMMISSION

Kathleen M.H. Wallman
Chief, Common Carrier Bureau

[43] *See, e.g.*, Ameritech Tariff FCC No. 1, Transmittal No. 823 (September 26, 1994) at 2; NYNEX Tariff FCC No. 1, Transmittal No. 333 (September 26, 1994) at 4; Bell Atlantic Tariff FCC No. 1, Transmittal No. 698 (September 26, 1994) at 2.

[44] *See supra* ¶ 3.

[45] *Third Report and Order*, 9 FCC Rcd at 2725, ¶ 27.

[46] Southwestern Bell Reply at 5.

[47] *Third Report and Order*, 9 FCC Rcd at 2725, ¶ 27.

[48] *See supra* ¶ 3.

Before the
Federal Communications Commission
Washington, D.C. 20554

CC Docket No. 94-97

In the Matter of

Southwestern Bell Telephone Company
Revisions to Tariff F.C.C. No. 73
Transmittal No. 2396

MEMORANDUM OPINION AND ORDER

Adopted: November 9, 1994; Released: November 10, 1994

By the Acting Chief, Tariff Division:

1. On November 7, 1994, Southwestern Bell Telephone Company (Southwestern Bell) filed Transmittal No. 2396 to revise its Tariff F.C.C. No. 73. Southwestern Bell states that the purpose of this filing is to amend material it originally filed under Transmittal No. 2382, which is Southwestern Bell's interim virtual collocation tariff.[1] Specifically, Southwestern Bell proposes to add to Tariff F.C.C. No. 73 the complete rate structure and rate levels for specific virtual collocation equipment. Southwestern Bell also proposes to revise Appendices B and C of its interim virtual collocaiton tariff. Southwestern Bell Telephone Company Transmittal No. 2396 at 1-2. No petitions were filed against this tariff. Transmittal No. 2396 scheduled to take effect on November 11, 1994.

2. This transmittal raises the same issues as the interim virtual collocation tariffs which were suspended for one day and made subject to investigation in the *Interim Tariff Suspension Order*.[2] Therefore, Transmittal No. 2396 is suspended for one day, until November 12, 1994, and will be subject to the investigation initiated in the *Interim Tariff Order*. These rates will also be subject to an accounting order to facilitate any refunds that may later prove necessary.

3. Accordingly, IT IS ORDERED that, pursuant to Section 204(a) of the Communications Act of 1934, 47 U.S.C. § 204(a), and Section 0.291 of the Commission's Rules, 47 C.F.R. § 0.291, the revisions to Southwestern Bell Telephone Company Tariff F.C.C. No. 73, Transmittal No. 2396, ARE SUSPENDED for one day and an investigation of the referenced tariff transmittal IS INSTITUTED.

4. IT IS FURTHER ORDERED that Southwestern Bell SHALL FILE tariff revisions within five business days of the release date of this Order to reflect this suspension.

5. IT IS FURTHER ORDERED that, for these purposes, we waive Sections 61.56, 61.58 and 61.59 of the Commission's Rules, 47 C.F.R. §§ 61.56, 61.58, and 61.59. Southwestern Bell should cite the "DA" number of the instant Order as the authority for this filing.

6. IT IS FURTHER ORDERED that, pursuant to Section 204(a) of the Communications Act of 1934, 47 U.S.C. § 204(a), Southwestern Bell shall keep accurate account of all amounts received by reason of the rates that are the subject of this investigation.

FEDERAL COMMUNICATIONS COMMISSION

Geraldine A. Matise
Acting Chief, Tariff Division
Common Carrier Bureau

[1] On July 25, 1994, the Commission released the *Virtual Collocation Order*, which required Tier local exchange carriers (LECs) (other than NECA pool members) to file virtual collocation tariffs on September 1, 1994, with a scheduled effective date of December 15, 1994. Expanded Interconnection with Local Telephone Company Facilities, CC Docket No. 91-141, Memorandum Opinion and Order, 9 FCC Rcd 5154 (1994), *appeal docketed sub nom.*, Southwestern Bell Telephone Company v. FCC, Case No. 94-1547 (D.C. Cir. Aug. 10, 1994) (*Virtual Collocation Order*). In conjunction with the *Virtual Collocation Order*, the Commission and the Tier 1 LECs reached an agreement whereby the LECs agreed to file "interim" virtual collocation tariffs on September 1, 1994 in order to facilitate the transition from physical to virtual collocation and to ensure that some form of collocation service was available at all times to interested customers. Following a one-day suspension period and the imposition of an accounting order, the interim tariffs became effective, subject to investigtion, on September 4, 1994. Ameritech Operating Companies *et al*, Order, 9 FCC Rcd 5230 (Com. Car. Bur. 1994) (*Interim Tariff Suspension Order*).

[2] *See Interim Tariff Suspension Order*, 9 FCC Rcd at 5321 (para. 6).

Before the
Federal Communications Commission
Washington, D.C. 20554

CC Docket No. 94-97

In the Matter of

BellSouth Telecomunications, Inc.
Revisions to Tariff F.C.C. No. 1
Transmittal No. 243

MEMORANDUM OPINION AND ORDER

Adopted: November 21, 1994; Released: November 22, 1994

By the Acting Chief, Tariff Division:

1. On November 21, 1994, BellSouth Telecomunications, Inc. (BellSouth) filed Transmittal No. 243 to revise its Tariff F.C.C. No. 1. BellSouth states that the purpose of this filing is to amend material it originally filed under Transmittal No. 222, which is BellSouth's interim virtual collocation tariff.[1] Specifically, BellSouth proposes to reduce the charges for the cross-connect rate elements and to include a service outage credit for the cross-connect elements when the cross-connects are inoperative. BellSouth also proposes to remove the provision that prohibits shared network arrangements in association with expanded interconnection service. Transmittal No. 243 is scheduled to take effect on November 24, 1994.

2. This transmittal raises the same issues as the interim virtual collocation tariffs which were suspended for one day and made subject to investigation in the *Interim Tariff Suspension Order*.[2] Therefore, Transmittal No. 243 is suspended for one day, until November 25, 1994, and will be subject to the investigation initiated in the *Interim Tariff Order*. These rates will also be subject to an accounting order to facilitate any refunds that may later prove necessary.

3. Accordingly, IT IS ORDERED that, pursuant to Section 204(a) of the Communications Act of 1934, 47 U.S.C. § 204(a), and Section 0.291 of the Commission's Rules, 47 C.F.R. § 0.291, the revisions to BellSouth Tariff F.C.C. No. 1, Transmittal No. 243, ARE SUSPENDED for one day and an investigation of the referenced tariff transmittal IS INSTITUTED.

4. IT IS FURTHER ORDERED that BellSouth SHALL FILE tariff revisions within five business days of the release date of this Order to reflect this suspension.

5. IT IS FURTHER ORDERED that, for these purposes, we waive Sections 61.56, 61.58 and 61.59 of the Commission's Rules, 47 C.F.R. §§ 61.56, 61.58, and 61.59. BellSouth should cite the "DA" number of the instant Order as the authority for this filing.

6. IT IS FURTHER ORDERED that, pursuant to Section 204(a) of the Communications Act of 1934, 47 U.S.C. § 204(a), BellSouth shall keep accurate account of all amounts received by reason of the rates that are the subject of this investigation.

FEDERAL COMMUNICATIONS COMMISSION

Geraldine A. Matise
Acting Chief, Tariff Division
Common Carrier Bureau

[1] On July 25, 1994, the Commission released the *Virtual Collocation Order*, which required Tier 1 local exchange carriers (LECs) other than NECA pool members to file virtual collocation tariffs on September 1, 1994, with a scheduled effective date of December 15, 1994. Expanded Interconnection with Local Telephone Company Facilities, CC Docket No. 91-141, Memorandum Opinion and Order, 9 FCC Rcd 5154 (1994), *appeal docketed sub nom.*, Southwestern Bell Telephone Company v. FCC, Case No. 94-1547 (D.C. Cir. Aug. 10, 1994) (*Virtual Collocation Order*). In conjunction with the *Virtual Collocation Order*, the Commission and the Tier 1 LECs reached an agreement whereby the LECs agreed to file "interim" virtual collocation tariffs on September 1, 1994 in order to facilitate the transition from physical to virtual collocation and to ensure that some form of collocation service was available at all times to interested customers. Following a one-day suspension period and the imposition of an accounting order, the interim tariffs became effective, subject to investigation, on September 4, 1994. Ameritech Operating Companies *et al*, Order, 9 FCC Rcd 5230 (Com. Car. Bur. 1994) (*Interim Tariff Suspension Order*).

[2] *See Interim Tariff Suspension Order*, 9 FCC Rcd at 5321 (para. 6).

FEDERAL COMMUNICATIONS COMMISSION

Before the
Federal Communications Commission
Washington, D.C. 20554

PUBLIC NOTICE

Released: November 23, 1994

PLEADING CYCLE ESTABLISHED FOR COMMENTS ON NCTA'S MOTIONS TO DISMISS SECTION 214 APPLICATIONS

On November 21, 1994, the National Cable Television Association, Inc. (NCTA) filed eight separate motions seeking to dismiss certain Section 214 applications for authority to construct, operate, own, and maintain video dialtone (VDT) systems. Specifically, NCTA requests that the Commission dismiss the Section 214 applications of 1) Ameritech Operating Companies (W-P-C-6927, W-P-C-6928, W-P-C-6926, W-P-C-6924, and W-P-C-6930); 2) Pacific Bell (W-P-C-6913, W-P-C-6914, W-P-C-6915, and W-P-C- 6916); 3) New England Telephone and Telegraph Company (W-P-C-6982 and W-P-C-6983); 4) GTE Virginia Inc. (W-P-C-6955), GTE Florida, Inc. (W-P-C-6956), GTE California, Inc. (W-P-C-6957), and GTE Hawaiian Telephone Company, Inc. (W-P-C-6958); 5) BellSouth Telecommunications, Inc. (W-P-C-6977); 6) New Jersey Bell Telephone Company (W-P-C-6838); 7) The Chesapeake and Potomac Telephone Company of Maryland and Virginia (W-P-C-6912), and The Bell Atlantic Telephone Companies (C&P of Maryland and Virginia)(W-P-C-6966); and 8) The Chesapeake and Potomac Telephone Company of Virginia (C&P of Virginia) (W-P-C-6834). For administrative ease, we are issuing one public notice to establish a pleading cycle for each of these motions.

NCTA states that the Section 214 applications are virtually the only opportunity for the Commission to study in detail the telephone companies proposals for the construction and operation of the VDT network. NCTA argues that in light of the importance of this review, the Commission should scrutinize the applications closely to ensure compliance with the principles governing VDT.

Interested parties should file comments on these motions by **December 1, 1994,** and reply comments by **December 6, 1994,** with the Secretary, FCC, 1919 M Street, N.W., Washington, D.C. 20554. All filings should clearly identify by file number to which motions they pertain. Three copies should also be sent to Peggy Reitzel, Common Carrier Bureau, FCC, Room 544, 1919 M Street, N.W., Washington, D.C. 20554, and to the Commission's contractor for public service records duplication: ITS, Inc. 2100 M Street, N.W., Suite 140, Washington, D.C. 20037.

Copies of the motions can be obtained from ITS at (202) 857-3800. The motions also are available for review and photocopying at the FCC Public Reference Room, 6th Floor, 2025 M Street, N.W., Washington, D.C., from 8:30 -12:30 and 1:30 -3:00 Monday through Thursday.

We will treat this proceeding as non-restricted for purposes of the Commission's *ex parte* rules. *See generally* 47 C.F.R. §§ 1.1200-1.1216. For further information contact Peggy Reitzel, Policy and Program Planning Division of the Common Carrier Bureau, at (202) 418-1579.

Before the
Federal Communications Commission
Washington, D.C. 20554

CC Docket No. 94-139

In the Matter of

AT&T Communications
F.C.C. Tariff No. 1,
Transmittal No. 7322

MEMORANDUM OPINION AND ORDER SUSPENDING RATES

Adopted: November 28, 1994; Released: November 28, 1994

By the Chief, Common Carrier Bureau:

1. On August 1, 1994, AT&T Communications (AT&T) filed its Transmittal No. 7322 to increase certain mileage rates for Customer Dialed Calling Card Calls. This service is regulated under the AT&T price cap plan as a Basket 1 service. In this filing, AT&T included adjustments to its price cap indices (PCIs) for each basket of service rates to account for exogenous increases in its costs. No petitions were filed against this transmittal.

2. In its price cap decisions,[1] the Commission replaced cost-plus rate of return regulation with an incentives-based system of regulation that rewards companies that become more productive and efficient, while ensuring that they share productivity and efficiency gains with their ratepayers. The theory of price caps is to harness the profit-making incentives common to all businesses in a manner that will advance the public interest goals of just, reasonable, and nondiscriminatory rates, as well as a communications system that offers innovative, high quality services[2]

3. Thus, price caps rewards carriers whose performance exceeds a benchmark measure of efficiency improvements. The benchmark, known as the price cap index or PCI, is adjusted each year based on inflation in the economy (as measured by the Gross National Product Price Index, or GNP-PI), minus a productivity factor.[3] The productivity factor is set to reflect the amount that the historical productivity growth of the telephone industry has exceeded the productivity of the economy as a whole,[4] plus a 0.5 percent Consumer Productivity Dividend.[5] Taken together, these factors established a reasonable target of efficiency growth, based on historical trends. Carriers that are able to generate productivity gains in excess of the target are allowed to generate and keep earnings higher than those experienced under rate of return regulation. Carriers also benefit because price tcap regulation provides increased rate flexibility and is simpler to administer. Ratepayers benefit because the price cap mechanism includes components that reflect historical telecommunications industry productivity, and then requires them to out-perform historical trends. Generally, changes in costs are not relevant to price cap regulation. Carriers must control their costs if they are to remain profitable. In this way, ratepayers receive the benefits of improved efficiency and reduced rates.[6]

4. The Commission has identified certain narrowly limited cost changes, termed "exogenous," that can be used to adjust the PCI. Exogenous costs are triggered by administrative, legislative, or judicial actions that are beyond the control of the carriers, and not already reflected in the GNP-PI[7] adjustment in price cap formula[8] The Commission found that a decision not to recognize these costs in the PCI would either unjustly punish or reward the carrier by treating these uncontrollable changes as changes in the carrier's level of efficiency[9]

5. Statement of Financial Accounting Standard 112, "Standards for Employers' Accounting for Postemployment Benefits," (SFAS-112) requires that accounting for expenses for severance pay and other benefits for laid-off (or otherwise separated) workers be made on an accrual, rather than a cash or "pay as you go," basis. SFAS-112 is the forecasted liability applicable to the current work force. Beginning in 1993, SFAS-112 requires companies to take a one-time operating expense adjustment for expected future payments associated with anticipated corporate layoffs ("restructuring" or "downsizing" plans). These payments include salary continuation, supplemental unemployment benefits, severance benefits, disability related benefits (including workers' compensation), job training and counseling, and continuation of benefits such as health care and life insurance coverage.

6. The Commission has required carriers to adopt SFAS-112 for Part 32 accounting[10] We conclude that, pursuant to the court's holding in *Southwestern Bell Telephone Company v. FCC*,[11] that the SFAS-112 costs may be eligible for exogenous treatment.

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[1] *See* Policy and Rules Concerning Rates for Dominant Carriers, Report and Order and Second Further Notice, 4 FCC Rcd 2873 (*AT&T Price Cap Order), modified on recon.*, 6 FCC Rcd 665 (1991)(*AT&T Price Cap Reconsideration Order);* Policy and Rules Concerning Rates for Dominant Carriers, Second Report and Order, 5 FCC Rcd 6786 (1990) and Erratum, 5 FCC Rcd 7664 (1990)(*LEC Price Cap Order), modified on recon.*, 6 FCC Rcd 2637 (1991)(*LEC Price Cap Reconsideration Order), further recon.*, 6 FCC Rcd 4524 (1991)(*ONA Part 69 Order), second further recon.*, 7 FCC Rcd 5235 (1992), *aff'd, National Rural Telecom Ass'n v. FCC*, 988 F.2d 174 (D.C. Cir. 1993); Competition in the Interstate Interexchange Marketplace, Report and Order, 6 FCC Rcd 5880 (1991)(*Interexchange Order)* (further streamlining and removing from price cap regulation most of AT&T's business services), *on recon.*, 7 FCC Rcd 2677 (1992).

[2] *See AT&T Price Cap Order*, 4 FCC Rcd at 2876-77.

[3] The price cap rules mandate a productivity offset of 3 percent for AT&T.

[4] *AT&T Price Cap Order*, 4 FCC Rcd at 2989-97.

[5] *Id.* at 3001-2.

[6] *AT&T Price Cap Reconsideration Order*, 6 FCC Rcd at 665.

[7] The GNP-PI (Gross National Product Price Index) is a measure of inflation in the general economy.

[8] *LEC Price Cap Order*. 7 FCC Rcd at 6807, *citing AT&T Price Cap Order*, 4 FCC Rcd at 3187.

[9] *Id.*

[10] *RAO Letter 22*, 8 FCC Rcd 4111 (Acc. & Aud. Div., Com. Car. Bur. 1993).

[11] 28 F.3d 165, 169-70 (1994).

7. In its August 1, 1994 filing, AT&T claimed $228.207 million of SFAS-112 costs as exogenous[12] Of this amount, $227.149 million was attributed to Basket 1, while $.296 million and $.762 million were attributed to Baskets 2 and 3, respectively. Following extensive discussions with Commission staff, AT&T revised its SFAS-112 exogenous claim downward[13] AT&T now calculates that SFAS-112 will result in an increase of $201.2 million in AT&T's costs for price capped services rather than the $228.207 million reflected in Transmittal No. 7322. AT&T proposes to allocate this adjustment among the price cap baskets as follows: $200.2 million (Basket 1); $.3 million (Basket 2); and $.7 million (Basket 3).

8. The calculations underlying AT&T's estimate of the SFAS-112 exogenous adjustment are complex and based on numerous assumptions. Although we have reviewed Transmittal 7322 and its supporting documents and have engaged in lengthy discussions with AT&T, several issues remain unresolved. For example, we question several of the underlying assumptions and data used by AT&T to compute the amount of SFAS-112 expense that is not included in the price cap formula adjustment (GNP-PI). We also have outstanding questions concerning, *inter alia:* AT&T's methods of allocating its total SFAS-112 costs between its regulated and non-regulated operations; AT&T's study used to project employee terminations; and its methods for projecting separation benefits expenses. Accordingly, we conclude that an investigation of these claims is warranted.

9. Therefore, pursuant to Section 204(a) of the Communications Act[14] and Section 0.291 of the Commission's rules,[15] we hereby institute an investigation of AT&T's proposed tariff changes based on the PCI adjustments flowing from its implementation of SFAS-112. We suspend the effective date of the transmittal for one day, impose an accounting order, and initiate an investigation. Issues will be designated and a pleading cycle established in a subsequent order.

ORDERING CLAUSES

10. Accordingly, IT IS ORDERED that, pursuant to Section 204(a) of the Communications Act of 1934, 47 U.S.C. § 204(a), and Section 0.291 of the Commission's Rules, 47 C.F.R. § 0.291, the revised rates set forth in AT&T Communications Tariff F.C.C. No. 1, Transmittal No. 7322 ARE SUSPENDED for one day from the current effective date and an investigation of those rates is instituted. AT&T Communications SHALL FILE a supplement reflecting this suspension no later than 5 days from the release of this Order.

11. IT IS FURTHER ORDERED that, pursuant to Section 4(i) and 204(a) of the Communications Act of 1934, 47 U.S.C. §§ 154(i), 204(a), and Section 0.291 of the Commission's Rules, 47 C.F.R. § 0.291, AT&T Communications SHALL KEEP ACCURATE ACCOUNT of all amounts received that are associated with the rates that are the subject of this investigation.

12. IT IS FURTHER ORDERED that AT&T Communications SHALL INCLUDE A STATEMENT in all subsequent transmittals revising rates in Baskets 1, 2 or 3 indicating whether, and to what extent, the price change is predicated upon the exogenous cost claim set forth in Transmittal No. 7322[16]

FEDERAL COMMUNICATIONS COMMISSION

Kathleen M.H. Wallman
Chief, Common Carrier Bureau

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[12] According to AT&T's Transmittal, its total company 1993 SFAS-112 expenses are $2.1 billion. Of this amount, AT&T concluded that approximately $630 million was attributable to AT&T Communications, which is responsible for AT&T's interstate and intrastate telecommunications services. AT&T calculated the total interstate impact of SFAS-112 for AT&T Communications to be approximately $429 million. Of this $429 million, AT&T attributed approximately $200 million to non-price cap (streamlined) interstate services. AT&T Letter of June 21, 1994, from Judy Arenstein, Government Affairs Vice President to William F. Caton, Acting Secretary, Federal Communications Commission, App. 1, at 5.

[13] AT&T Letter of November 18, 1994, from M. F. Del Casino, Administrator-Rates and Tariffs to William F. Caton, Acting Secretary, Federal Communications Commission.

[14] 47 U.S.C. § 204(a).

[15] 47 C.F.R. § 0.291.

[16] We anticipate that any such transmittals will be suspended for one day, included in this investigation, and made subject to an accounting order.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

GRAPHNET, INC. File No. I-T-C-94-473

Application for authority to acquire and operate satellite facilities for provision of service to various overseas points.

ORDER, AUTHORIZATION AND CERTIFICATE

Adopted: November 23, 1994; Released: December 6, 1994

By the Chief, Telecommunications Division:

1. Upon consideration of the above-captioned uncontested application, IT IS HEREBY CERTIFIED that the present and future public convenience and necessity require a grant thereof.

2. Accordingly, IT IS ORDERED that application File No. I-T-C-94-473 IS GRANTED and Graphnet, Inc. (Graphnet) is authorized to:

a. lease from Comsat and operate the satellite circuits specified in Appendix A, between appropriately licensed U.S. earth stations and INTELSAT Atlantic and Pacific Ocean Region satellites, connecting with similar facilities between the satellites and the overseas points listed in Appendix A, furnished by its correspondents;

b. lease from PanAmerican Satellite Corp. (PAS) and operate the satellite circuits specified in Appendix B, between appropriately licensed U.S. earth stations and the PAS-1 satellite, connecting with similar circuits between the satellite and the overseas points listed in Appendix B, furnished by its correspondents;

c. lease from the Columbia/TDRSS International Satellite System (TDRSS) and operate the satellite circuits specified in Appendix C, between appropriately licensed U.S. earth stations and the TDRS-41 and TDRS-174 satellites, connecting with similar circuits between the satellites and the overseas points listed in Appendix C, furnished by its correspondents;

d. lease and operate one 1.544 Mbps satellite circuit to Mexico and Canada, respectively, routed via U.S. domestic satellites and Mexican domestic or Canadian domestic satellites, consistent with the Commission's transborder policy;

e. lease and operate one 1.544 terrestrial circuit to Mexico and Canada, respectively;

f. lease and operate necessary connecting facilities in the United States;

g. lease a one-half interest in and operate any necessary overseas connecting facilities; and

h. use the facilities authorized herein to provide regularly authorized services, including switched voice and data, and private line services, between the United States and the points specified in Appendices A, B, and C.

3. IT IS FURTHER ORDERED that neither Graphnet nor any persons or companies directly or indirectly controlling or controlled by Graphnet, or under direct or indirect common control with it, shall acquire or enjoy any right, for the purposes of handling or interchanging traffic to or from the United States, its territories or possessions, which is denied to any other United States carrier by reason of any concession, contract, understanding, or working arrangement to which Graphnet or any persons or companies controlling or controlled by Graphnet are parties.

4. IT IS FURTHER ORDERED that our authorization of Graphnet to provide private lines as part of its authorized services is limited to the provision of such private lines only between the United States and the countries listed in the Appendices – that is, private lines which originate in the United States and terminate in one of the countries listed in the Appendices or which originate in one of the countries listed in the Appendices and terminate in the United States. In addition, Graphnet may not – and Graphnet's tariff must state that its customers may not – connect private lines provided over these facilities to the public switched network at either the U.S. or foreign end, or both, for the provision of international basic telecommunications services, including switched voice services, unless authorized to do so by the Commission upon a finding that the destination country affords resale opportunities equivalent to those available under U.S. law, in accordance with *Regulation of International Accounting Rates, Phase II, First Report and Order,* 7 FCC Rcd 559 (1991), Order on Reconsideration and Third Further Notice of Proposed Rulemaking, 7 FCC Rcd 7927 (1994), *petition for reconsideration pending.*

5. IT IS FURTHER ORDERED that the applicant shall file copies of any operating agreements entered into with its foreign correspondents with the Commission within 30 days of their execution, and shall otherwise comply with the filing requirements contained in Section 43.51 of the Commission's Rules, 47 C.F.R. §43.51.

6. IT IS FURTHER ORDERED that the applicant shall file a tariff pursuant to Section 203 of the Communications Act, 47 U.S.C. §203 and Part 61 of the Commission's Rules, 47 C.F.R. Part 61, for the services authorized in this Order.

7. IT IS FURTHER ORDERED that the applicant shall file the annual reports of overseas telecommunications traffic required by Section 43.61 of the Commission's Rules, 47 C.F.R. §43.61.

8. IT IS FURTHER ORDERED that the applicant shall file a separate Section 214 application for any additional circuits it seeks to operate via the PAS-1, TDRS-41 or TDRS-174 satellites.

9. IT IS FURTHER ORDERED that the number of circuits authorized herein for the provision of services via separate satellite systems is subject to limitations on the

number of circuits specified under the separate systems policy and applicable consultations under Article XIV(d) of the INTELSAT Agreement.

10. This Order is issued under Section 0.261 of the Commission's Rules and is effective upon adoption. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the date of public notice of this Order (see Section 1.4(b)(2)).

FEDERAL COMMUNICATIONS COMMISSION

Diane J. Cornell
Chief, Telecommunications Division
International Bureau

APPENDIX A
INTELSAT FACILITIES

Authority is granted for one 1.544 Mbps circuit to each country marked with single *, six 64-kbps circuits to each country marked with a double **, and one 64-kbps circuit to each country not marked.

(1) Atlantic Ocean Region

Latin America

Antigua	Curacao	Netherlands Antilles
Argentina *	Dominican Rep. **	Nicaragua
Aruba	Ecuador	Panama **
Bahamas	El Salvador **	Paraguay
Barbados	French Guiana	Peru
Belize	Grenada	St. Lucia
Bermuda	Guantanamo Bay	St. Vincent
Bolivia	Guatemala	Surinam
Brazil *	Guyana	Trinidad & Tobago
Cayman Islands	Haiti	Turks & Caicos Islands
Chile *	Honduras	Uruguay
Colombia **	Jamaica	Venezuela *
Costa Rica	Martinique	

Europe

Austria **	Iceland	San Marino
Belgium *	Ireland **	Slovenia
Czech Republic *	Italy *	Spain *
Croatia	Liechtenstein	Sweden *
Cyprus	Luxembourg	Switzerland *
Denmark **	Malta	Turkey
Finland **	Monaco	United Kingdom *
France *	Netherlands *	Vatican City
Germany *	Norway **	Yugoslavia
Greece **	Portugal	

Middle East, Africa, Europe

Algeria	Canary Islands	Guinea
Angola	Cape Verde Is.	Hungary **
Armenia	Central African	Iran
Ascension Is.	Chad Rep.	Iraq
Ajerbaijan	Congo	Israel *
Azores	Diego Garcia	Ivory Coast
Bahrain **	Egypt **	Jordan
Belarus **	Estonia	Kazakhstan
Benin	Ethiopia	Kenya
Botswana	Gabon	Kuwait **
Bulgaria	Gambia	Kyrgystan
Burkina Faso	Georgia	Latvia
Burma	Ghana	Lebanon **

Cameroon
Liberia
Libya
Lithuania
Madagascar
Malagasy Rep.
Malawi
Mali
Mauritania
Moldova
Morocco
Mozambique
Niger
Nigeria
Oman
Gibraltar
Pakistan
Poland *
Qatar
Romania
Russian Fed. *
Saudi Arabia *
Senegal
Sierra Leone
South Africa
Sri Lanka
Sudan
Swaziland
Syria
Tajikistan
Lesotho
Tanzania
Togo
Tunisia
Turkmenistan
Uganda
Ukraine **
United Arab Emirates **
Uzbekistan
Yemen
Zaire
Zambia
Zimbabwe

(2) Pacific Ocean Region

American Samoa
Australia *
Brunei
China (Peoples' * (Rep.)
Christmas Is.
Cook Islands
Ebeye
Fiji Islands
French Polynesia
Guam
Hong Kong *
India *
Indonesia *
Japan *
Kiribati
Korea (Rep. of) *
Kosrae
Majuro
Malaysia *
Mariana Islands
Nauru
New Caledonia
New Guinea
New Zealand
Palau
Papua New Guinea
Philippines *
Ponape
Saipan
Singapore *
Solomon Islands
Sri Lanka
Taiwan *
Thailand
Tonga
Truk
Vanuatu
Western Samoa
Yap

APPENDIX B
PAS-1 CIRCUITS

Authority is granted for one 64-kbps circuit to each of the following points, NOT INTERCONNECTED with the public switched network:

Ku-Band countries

Albania
Anguilla
Armenia
Austria
Azerbaijan
Bahamas
Belarus
Belgium
Bermuda
Bulgaria
British Virgin Is.
Cayman Islands
Czech Republic
Denmark
Estonia
France
Georgia
Germany
Greece
Hungary
Ireland
Italy
Kazakhstan
Kyrgyzstan
Latvia
Lithuania
Luxembourg
Moldova
Monaco
Montserrat
Netherlands
Poland
Portugal
Romania
Russian Federation
Slovenia
Spain
Sweden
Switzerland
Tajikistan
Turkmenistan
Turks & Caicos Is.
Ukraine
United Kingdom
Uzbekistan
Yugoslavia

C-band countries

Anguilla
Antigua
Argentina
Aruba
Bahamas
Barbados
Barbuda
Belize
Bermuda
Bolivia
Brazil
British Virgin Is.
Cayman Islands
Chile
Colombia
Costa Rica
Dominica
Dominican Rep.
Ecuador
Grenada
Guatemala
Guyana
Haiti
Honduras
Jamaica
Mexico
Montserrat
Netherlands Antilles
Panama
Paraguay
Peru
St. Christopher & Nevis
St. Lucia
St. Vincent & Grenadines
Suriname
Trinidad & Tobago
Turks & Caicos Islands
Uruguay
Veneuela

Authority is granted for six 64-kbps circuits to each of the following points, INTERCONNECTED with the public switched network:

Ku-band countries

Albania	Georgia	Portugal
Armenia	Hungary	Romania
Azerbaijan	Kazakhstan	Russian Federation
Bahamas	Kyrgyzstan	Slovenia
Belarus	Latvia	Tajikistan
Bulgaria	Lithuania	Turkmenistan
Czech Republic	Moldova	Ukraine
Estonia	Poland	United Kingdom
		Uzbekistan

C-band countries

Bahamas	Dominican Rep.	Panama
Costa Rica	Netherlands Ant.	Peru

APPENDIX C
TDRS CIRCUITS

Authority is granted for one 64-kbps circuit to each of the following points, NOT INTERCONNECTED with the public switched network:

TDRS-41

Austria	Germany	Netherlands
Bahamas	Ireland	Portugal
Belgium	Israel	Sweden
Canada	Jamaica	Switzerland
Denmark	Liechtenstein	Turkey
Finland	Luxembourg	United Kingdom
France	Mexico	

TDRS-174

Hong Kong
Mexico
Philippines

Authority is granted for six 64-kbps circuits to each of the following points, INTERCONNECTED with the public switched network:

TDRS-41	TDRS-174
United Kingdom	Hong Kong

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

GLOBETEL, INC. File No. I-T-C-94-487

Application for authority to
acquire and operate facilities
for provision of INTELSAT Business
Services, INTELNET Service and
International Television Service,
and to resell switched voice
services.

ORDER, AUTHORIZATION AND CERTIFICATE

Adopted: November 23, 1994; Released: December 6, 1994

By the Chief, Telecommunications Division:

1. Upon consideration of the above-captioned uncontested application, filed pursuant to Section 214 of the Communications Act of 1934, as amended, IT IS HEREBY CERTIFIED that the present and future public convenience and necessity require a grant thereof.

2. Accordingly, IT IS ORDERED that application File No. I-T-C-94-487 IS GRANTED, and Globetel, Inc. (Globetel) is authorized to:

a. establish channels of communication between appropriately licensed U.S. earth stations and appropriate INTELSAT Atlantic and Pacific Ocean Region satellites, for the provision of INTELSAT Business Services(IBS), International Television Service and INTELNET Service between the United States and the points listed in Comsat's Tariff for the space segment of these services;

b. acquire and operate capacity in the appropriately licensed U.S. earth stations, to be used in conjunction with the space segment capacity;

c. use the facilities in a. and b. above to provide IBS, International Television Service and INTELNET service; and

d. provide international switched services by the resale of the international switched voice services set forth in AT&T's Tariff FCC No. 1, MCI's Tariff FCC No. 1, Sprint's Tariffs FCC Nos. 1 and 2, and Worldcom's Tariff FCC No. 1, between the United States and the points listed in those tariffs.

3. IT IS FURTHER ORDERED that neither Globetel nor any persons or companies directly or indirectly controlling or controlled by Globetel, or under direct or indirect common control with it, shall acquire or enjoy any right, for the purposes of handling or interchanging traffic to or from the United States, its territories or possessions, which is denied to any other United States carrier by reason of any concession, contract, understanding, or working arrangement to which Globetel or any persons or companies controlling or controlled by Globetel are parties.

4. IT IS FURTHER ORDERED that the applicant shall file copies of any operating agreements it enters into with its foreign correspondent with the Commission within 30 days of its execution, and shall otherwise comply with the filing requirements contained in Section 43.51 of the Commission's Rules, 47 C.F.R. §43.51.

5. IT IS FURTHER ORDERED that the applicant shall file a tariff pursuant to Section 203 of the Communications Act, 47 U.S.C. §203, and Part 61 of the Commission's Rules, 47 C.F.R. Part 61, for the services authorized in this Order.

6. IT IS FURTHER ORDERED that the applicant shall file the annual reports of overseas telecommunications traffic required by Section 43.61 of the Commission's Rules, 47 C.F.R. §43.61.

7. The Commission retains jurisdiction over this matter to reallocate circuits in the satellite system among the various international common carriers and other authorized users as required to ensure nondiscriminatory use of, and equitable access to, the communications satellite system.

8. This order is issued under Section 0.261 of the Commission's Rules and is effective upon adoption. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the date of public notice of this order (*see* Section 1.4(b)(2)).

FEDERAL COMMUNICATIONS COMMISSION

Diane J. Cornell
Chief, Telecommunications Division
International Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

AMERICAN TELEPHONE AND TELEGRAPH COMPANY

File No. I-T-C-94-494

Application for authority to convey capacity in the TCS-1 Cable System.

ORDER AND AUTHORIZATION

Adopted: November 23, 1994; Released: December 6, 1994

By the Chief, Telecommunications Division:

1. Upon consideration of the above-captioned uncontested application, filed pursuant to Section 214 of the Communications Act of 1934, as amended, we find that the present and future public convenience and necessity require a grant thereof.

2. Accordingly, IT IS ORDERED that application File No. I-T-C-94-494 IS GRANTED, and American Telephone and Telegraph Company (AT&T) is authorized to:

a. convey to IDB WorldCom on an Indefeasible Right of User (IRU) basis a one-half interest in 24 MAUOs[1] in the Florida-Puerto Rico and Puerto Rico-Dominican Republic subsegments of the TCS-1 Cable System; and

b. convey to Mercury Communications Ltd. on an IRU basis a one-half interest in 30 MAUOs in the Puerto Rico-Dominican Republic and Dominican Republic-Jamaica subsegments of the TCS-1 Cable System.

3. This Order is issued under Section 0.261 of the Commission's Rules and is effective upon adoption. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the date of public notice of this Order (see Section 1.4(b)(2)).

FEDERAL COMMUNICATIONS COMMISSION

Diane J. Cornell
Chief, Telecommunications Division
International Bureau

[1] A Minimum Assignable Unit of Ownership (MAUO) is a 64-kbps circuit equivalent.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

AMERICAN TELEPHONE AND TELEGRAPH COMPANY

File No. I-T-C-94-495

Application for authority to acquire and operate facilities in the CARAC Cable System.

FEDERAL COMMUNICATIONS COMMISSION

Diane J. Cornell
Chief, Telecommunications Division
International Bureau

ORDER AND AUTHORIZATION

Adopted: November 23, 1994; Released: December 6, 1994

By the Chief, Telecommunications Division:

1. Upon consideration of the above-captioned uncontested application, filed pursuant to Section 214 of the Communications Act of 1934, as amended, we find that the present and future public convenience and necessity require a grant thereof.

2. Accordingly, IT IS ORDERED, that application File No. I-T-C-94-495 IS GRANTED, and American Telephone and Telegraph Company (AT&T) is authorized to:

a. acquire on an Indefeasible Right of User (IRU) basis, activate and operate 30 half-Basic Units[1] of capacity in the Caribbean-Atlantic (CARAC) Cable System;

b. acquire and operate any necessary overseas connecting facilities;

c. use said facilities to provide AT&T's regularly authorized services between the United States and Bermuda; and

d. multiply, by the use of Digital Circuit Multiplication Equipment (DCME), the bearer circuits authorized herein to obtain the maximum obtainable number of circuits.

3. IT IS FURTHER ORDERED that the authority herein is granted subject to the terms and conditions set forth in the C&MAs for the CARAC Cable Systems, as well as any Commission Order granting authority to acquire and operate facilities in the CARAC Cable System.

4. This Order is issued under Section 0.261 of the Commission's Rules and is effective upon adoption. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the date of public notice of this Order (see Section 1.4(b)(2)).

[1] As described in the CARAC Construction and Maintenance Agreement, "A Basic Unit (also known as a DS-0) shall consist of a 64,000 bits per second both way digital line link with interface in accordance with CCITT Recommendation G.703 passing through two CARAC System Interface Points. Each CARAC System Basic Unit shall comprise two half circuits (henceforth referred to as half-Basic Units), a northern half-Basic Unit and a corresponding southern half-Basic Unit."

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

AMERICAN TELEPHONE AND TELEGRAPH COMPANY

File No. I-T-C-94-510

Application for authority to convey capacity in the TAT-9 Cable System.

ORDER AND AUTHORIZATION

Adopted: November 23, 1994; Released: December 6, 1994

By the Chief, Telecommunications Division:

1. Upon consideration of the above-captioned uncontested application, filed pursuant to Section 214 of the Communications Act of 1934, as amended, we find that the present and future public convenience and necessity require a grant thereof.

2. Accordingly, IT IS ORDERED that application File No. I-T-C-94-510 IS GRANTED, and American Telephone and Telegraph Company (AT&T) is authorized to:

a. convey to its correspondent in Bangladesh on an Indefeasible Right of User (IRU) basis a one-half interest in 30 MAUOs[1] in the TAT-9 Cable System between Manahawkin, New Jersey and Goonhilly, United Kingdom; and

b. convey to TRT/FTC Communications, Inc. on an IRU basis a one-half interest in 60 MAUOs in the TAT-9 Cable System between Manahawkin, New Jersey and St Hilaire, France;

3. This Order is issued under Section 0.261 of the Commission's Rules and is effective upon adoption. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the date of public notice of this Order (see Section 1.4(b)(2)).

FEDERAL COMMUNICATIONS COMMISSION

Diane J. Cornell
Chief, Telecommunications Division
International Bureau

[1] A Minimum Assignable Unit of Ownership (MAUO) is a 64-kbps circuit equivalent.

Before the
Federal Communications Commission
Washington, D.C. 20554

In re:

Complaint of Lightning Broadcasting Corporation against Douglas Cable Communications	CSR-4264-M

Request for Carriage

MEMORANDUM OPINION AND ORDER

Adopted: November 21, 1994; Released: December 7, 1994

By the Chief, Cable Services Bureau:

1. On June 6, 1994, a complaint on behalf of Lightning Broadcasting Company ("LBC"), licensee of low power television Station W41BL (Channel 41), Effingham, Illinois, was filed with the Commission claiming that Douglas Cable Communications ("Douglas Cable"), operator of cable television systems serving Beecher City, Cowden, Edgewood, and Mason, Illinois, had declined to carry the station, even though W41BL is a fully-qualified low power television station within the meaning of §76.56(b)(3) of the Commission's Rules and §§614(c) and (h)(2) of the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992). No opposition to this complaint has been filed.

2. In support of its complaint, LBC argues that W41BL: 1) is a 24-hour per day low power television station broadcasting from a transmitter located at north latitude 39°16'19", west longitude 88°30'32"; 2) is located within 35 miles of Douglas Cable's principal headends for the Beecher City, Cowden, and Edgewood cable systems,[1] all of which are located in Effingham County, Illinois; 3) is in full compliance with Part 73 of the Commission's rules governing children's programming, political broadcasting and Equal Employment Opportunity; 4) Effingham, its community-of-license, has a population of 11,851 and is not located within the 160 largest metropolitan statistical areas; 5) provides locally-originated programming; and 6) there are no full power television stations licensed to the county served by Douglas Cable, Effingham County. LBC states that it notified Douglas Cable of its obligation to carry W41BL on April 8, 1994, and that Douglas Cable did not respond to LBC's notice within the 30 day period required by the Commission's Rules. LBC further states that Douglas Cable's Beecher City, Cowden, and Edgewood systems have adequate channel capacity to carry one qualified low power television station.[2]

3. Section 614(a) of the Communications Act of 1934, as amended, requires the carriage of "qualified" low power television (LPTV) stations in certain limited circumstances. *See* 47 U.S.C. §534(a). An LPTV station that conforms to the rules established for LPTV stations in Part 74 of the Commission's Rules will be considered "qualified" only if: (1) if broadcasts for at least the minimum number of hours of operation required under 47 C.F.R. Part 73; 2) it adheres to Commission requirements regarding non-entertainment programming and employment practices;[3] 3) it complies with interference regulations consistent with its secondary status; 4) it is located no more than 35 miles from the cable system's headend and delivers to the principal headend an over-the-air signal of good quality; 5) the community of license of the station and the franchise area of the cable system are both located outside the largest 160 Metropolitan Statisticalp Areas (MSA's) on June 30, 1990, and the population of such community of license on that date did not exceed 35,000; and 6) there is no full power television broadcast station licensed to any community within the county or other political subdivision (of a State) served by the cable system. *See* 47 U.S.C. §534(h)(2); 47 C.F.R. §76.55(d).

4. The facts as stated by LBC in its complaint and its notice to Douglas Cable indicate that W41BL is a qualified LPTV within the meaning of §76.56(b)(3) of the Commission's Rules and §§614(c) and (h)(2) of the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992). Because Douglas Cable has not filed a response to LBC's complaint, we find, based on the facts as presented in LBC's complaint, that W41BL is a qualified low power station and that it is entitled to carriage on Douglas Cable's Beecher City, Cowden, Edgewood, and Mason, Illinois systems. Accordingly, the Complaint filed June 6, 1994, by Lightning Broadcasting Company IS GRANTED pursuant to §614(c) (47 U.S.C. §534(c)) of the Communications Act of 1934, as amended, and Douglas Cable IS ORDERED to commence carriage of low power television Station W41BL forty-five (45) days from the release date of this Order. This action is taken by the Chief, Cable Services Bureau, pursuant to delegated authority.

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[1] The Edgewood system also serves Mason, Illinois.

[2] LBC states that the *1993 Television and Cable Factbook* indicates that Douglas Cable has a channel capacity of 17 channels on its Beecher City system, 35 channels on its Cowden system, and 21 channels on its Edgewood system.

[3] Section 614(h)(2)(B) provides that the LPTV station must meet "all obligations and requirements applicable to television broadcast stations under Part 73 of Title 47, Code of Federal Regulations, with respect to the broadcast of nonentertainment programming; programming and rates involving political candidates, election issues, controversial issues of public importance, editorials, and personal attacks; programming for children; and equal employment opportunity; and the Commission [must] determine that the provision of such programming by such station would address local news and informational needs which are not being adequately served by full power television broadcast stations because of geographic distance of such full power stations from the low power station's community of license." 47 U.S.C. §534(h)(2)(B); 47 C.F.R. §76.55(d).

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

STAR CABLE ASSOCIATES

Petition for Reconsideration

of Certification of
Carroll County, Virginia
to Regulate Basic Cable Rates
(VA0446)

MEMORANDUM OPINION AND ORDER

Adopted: November 28, 1994; Released: November 29, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On December 13, 1993, Star Cable Associates ("Star Cable") filed a timely petition for reconsideration challenging the certification of Carroll County, Virginia to regulate rates for basic cable service and associated equipment.[1] In addition, Star Cable submitted responses to the Bureau's oral requests for clarification. Carroll County did not file an opposition to Star Cable's petition.

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[2] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless the franchising authority has actual knowledge to the contrary.[3] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[4] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days of the effective date of certification.[5] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[6]

II. DISCUSSION

3. Star Cable argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in the unincorporated areas of Carroll County, the franchise area.[7] Star Cable claims that it currently serves only 357 of the 9,580 households (that is, occupied housing units)[8] in the franchise area, or 4 percent of the total number of households. As supporting documentation, Star Cable provides 1990 Census data[9] which shows that there are 9,580 households in the unincorporated areas of Carroll County. Star Cable also submits a computer print-out with sufficient subscriber information to support its claim that it serves 357 households in the franchise area. Finally, Star Cable provides an affidavit by a responsible official certifying the accuracy of the data included in the petition.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[10] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[11] Star Cable has met this burden. Star Cable appropriately relied on data reflecting the number of households as required by our rules.[12] Relying on this data, Star Cable has submitted sufficient evidence demonstrating that its cable system serving Carroll County serves 357 of the 9,580 households, or 4 percent of the households, within its franchise area. Thus, we find that Star Cable's system serving the unincorporated areas of Carroll County is subject to effective competition. Accordingly, its petition is granted.

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[1] Carroll County filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on October 18, 1993, which became effective on November 17, 1993.

[2] 47 U.S.C. § 543(a)(4).

[3] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[4] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition. 47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[5] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking,* MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[6] 47 C.F.R. § 76.911(c).

[7] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30% of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[8] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration,* MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*Third Recon. Order).* The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[9] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates,* 9 FCC Rcd 3656 (1994).

[10] 47 C.F.R. § 76.906.

[11] 47 C.F.R. § 76.911(b)(1).

[12] *See Third Recon. Order, supra.*

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Star Cable challenging the certification of Carroll County, Virginia to regulate Star Cable's basic cable rates IS GRANTED.

6. IT IS FURTHER ORDERED that the certification of Carroll County to regulate Star Cable's basic cable rates IS RESCINDED.

7. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

PP Docket No. 93-253

In the Matter of

Implementation of Section 309(j)
of the Communications Act -
Competitive Bidding

SECOND MEMORANDUM OPINION AND ORDER

Adopted: August 12, 1994; Released: August 15, 1994

By the Commission:

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I. INTRODUCTION

1. By this action, we respond to petitions for reconsideration or clarification of the rules and policies adopted in the *Second Report and Order* in this proceeding, which sets forth general rules for the use of competitive bidding to award licenses.[1] Twenty-one such petitions were received, as well as eight oppositions and five replies. A list of the petitions, oppositions and replies is contained in Appendix A.

2. On August 10, 1993, the Omnibus Budget Reconciliation Act of 1993 (the Budget Act) added Section 309(j) to the Communications Act of 1934, as amended, 47 USC §309(j).[2] Section 309(j) gives the Commission express authority to employ competitive bidding procedures to choose among mutually exclusive applications for initial licenses. The Commission adopted a *Notice of Proposed Rulemaking* in this proceeding on September 23, 1993.[3] The *Second Report and Order* prescribing the required regulations was adopted on March 8, 1994. The Commission has subsequently adopted specific rules for auction of

[1] *Second Report and Order*, PP Docket No. 93-253, 9 FCC Rcd 2348, 59 FR 22980 (May 4, 1994) (*Second Report and Order*).

[2] *See* Omnibus Budget Reconciliation Act of 1993, 47 U.S.C. 309(j)(3)(B).

[3] *Notice of Proposed Rule Making* in PP Docket No. 93-253, 8 FCC Rcd 7635, 58 FR 53489 (Oct 15, 1993), (*NPRM*). In the *First Report and Order* in PP Docket No. 93-253, FCC 94-32, released February 4, 1994, 59 FR 09100 (Feb 25, 1994), (*First Report and Order*), the Commission prescribed transfer disclosure requirements with respect to licenses awarded by random selection.

narrowband Personal Communications Service (PCS) licenses,[4] Interactive Video and Data Service (IVDS) licenses,[5] and broadband PCS licenses.[6]

3. The *Second Report and Order* established rules for determining what types of services and licenses may be subject to auctions. The *Second Report and Order* also set forth a range of auction designs and procedures, from which the Commission stated it would choose in establishing procedures for awarding licenses in specific services. The *Second Report and Order* addressed avariety of procedural issues regarding announcement of auctions, filing of applications, bidder and licensee qualifications, payment requirements, and penalties for default or disqualification, as well as safeguards to deter possible abuses of the bidding and licensing process. In response to statutory directive, the *Second Report and Order* also identified provisions designed to ensure that small businesses, rural telephone companies, and businesses owned by women or members of minority groups (designated entities) are given the opportunity to participate in the provision of spectrum-based services.

4. In many cases, the appropriate auction procedures and rules vary from service to service. In the *Second Report and Order* we retained the flexibility to choose, from within a defined range, the appropriate procedures for particular services, depending on characteristics of the service such as the likely value and interdependence of the licenses being auctioned and the capital required to construct a system. We also retained the flexibility to alter our procedures in response to our experience with different auction techniques.

5. We dispose of all but two of the petitions for reconsideration of the *Second Report and Order* in this Order. We defer consideration of Brown and Schwaninger's petition concerning Finders's Preferences. We plan to issue a Further Notice addressing the applicability of Finder's Preferences to auctionable services in the near future, and we will consider Brown and Schwaninger's petition in the context of that Notice. We also defer to a future Order consideration of MCI's petition concerning auctioning of BETRS licenses.

6. The issues raised in the petitions for reconsideration fall into three categories: those dealing with the applicability of competitive bidding to specific services and particular circumstances, those dealing with auction design and procedures, and those dealing with the definition of the groups eligible for special provisions (the "designated entities") and the nature of these provisions. We consider issues raised by these petitions below.

II. APPLICABILITY OF COMPETITIVE BIDDING

A. Cellular Unserved Areas

7. Two cellular systems operate on separate frequency blocks in each cellular market.[7] The geographic areas not covered after five years by the initial licensees are considered cellular "unserved areas" that are licensed separately. In 1991, we adopted random selection procedures to govern licensing of the cellular unserved areas,[8] and stated that we would revisit this decision to use lotteries if Congress authorized Commission use of competitive bidding procedures.[9] As noted above, competitive bidding authority was in fact enacted in 1993.[10]

8. After receiving comment and considering the extensive record, the Commission indicated in the *Second Report and Order* that, unless specifically excluded, mutually exclusive applications for licenses in the Public Mobile Services, including the Cellular Service, will be subject to competitive bidding if they were filed after July 26, 1993.[11] We noted, however, that applications filed before July 26, 1993 present special issues due to the "special rule" of Section 6002(e) of the Budget Act.[12] That rule does not require the Commission to award licenses or permits by competitive bidding if the license applications were filed before July 26, 1993, even if the applications otherwise meet the criteria that would subject them to selection by bidding.[13] We therefore stated in the Second Report and Order that we would determine in a separate order how to authorize Public Mobile systems if applications were filed before July 26, 1993.[14] Subsequently, after thorough consideration of the record, we adopted a Memorandum Opinion and Order stating that in such situations we will award licenses for the unserved areas by random selection.[15]

9. *Petitions.* We received three petitions for reconsideration of th e provisions of the Second Report and Order related to authorization of the cellular unserved areas.[16] John G. Andrikopoulos, et al. (Andrikopoulos) states that where applications for cellular unserved area licenses were accepted for filing before July 26, 1993, the applications should not be subject to competitive bidding. Andrikopoulos asserts that auctioning these licenses would be unreasonable, retroactive application of the Budget Act.[17] The Houston, Dallas, Oxnard and Huntington Cellular Settlement Groups (Cellular Settlement Groups; Groups) assert that the Commission should accept full-market settlements between mutually exclusive applicants for cellular unserved area licenses.[18] These Groups state that Congress intended the Commission to continue use of its existing policy favoring full-market settlements, and ex-

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[4] *Third Report and Order* in PP Docket No. 93-253, 9 FCC Rcd 2941, 59 FR 26741 (May 24, 1994)(*Third Report and Order*).

[5] *Fourth Report and Order* in PP Docket No. 93-253, 59 FR 24947 (May 13, 1994) (*Fourth Report and Order*).

[6] *Fifth Report and Order* in PP Docket No. 93-253, FCC 94-178, 59 FR 37566 (Jul 29, 1994) adopted June 29, 1994, released July 15, 1994 (*Fifth Report and Order*).

[7] The Domestic Public Cellular Service is governed by Part 22 of the Commission's Rules, 47 CFR Part 22.

[8] See *First Report and Order and Memorandum Opinion and Order on Reconsideration,* CC Docket No. 90-6, 6 FCC Rcd 6185, 56 FR 58503 (Nov 20, 1991).

[9] *Id.* at 6217.D

[10] *See* Budget Act, 107 Stat. 387-392.

[11] See Second Report and Order at ¶ 61 & n.58.

[12] *See* id. at n.55, citing Budget Act, § 6002(e).

[13] See Budget Act, § 6002(e).

[14] See Second Report and Order at n.55.

[15] See Memorandum Opinion and Order, PP Docket No. 93-253, FCC No. 94-123, 59 FR 37163 (Jul 21, 1994), adopted May 27, 1994, released July 14, 1994 (*Memorandum Opinion and Order*).

[16] See petitions of Thumb Cellular Limited Partnership (Thumb Cellular), John Andrikopoulos, et al . (Andrikopoulos), and cellular settlement groups in Houston, Dallas, Oxnard and Huntington (Cellular Settlement Groups).

[17] See Andrikopoulos Petition at 4-5.

[18] See Cellular Settlement Groups Petition at 3-7.

press concern that the Second Report and Order appears to prohibit full-market settlements where licenses will be awarded through competitive bidding procedures.[19] Finally, Thumb Cellular, a party to a full-market settlement agreement filed for a Detroit unserved area, asks the Commission to process its settlement agreement immediately.[20]

10. *Discussion.* The issues raised by these petitioners are fully addressed in the Memorandum Opinion and Order, which was released shortly after these petitions were filed. We stated in that item that we will grant licenses for cellular unserved areas by random selection from the pool of applicants that filed lottery applications prior to July 26, 1993, and we will permit full-market settlements among lottery applicants to avoid mutual exclusivity.[21] Applications for cellular unserved areas accepted for filing prior to July 26, 1993 will not be subject to competitive bidding. Accordingly, the issues raised by these three petitioners are moot.

B. Principal Use of PCS

11. Section 309(j)(1) of the Communications Act, as amended, permits auctions only where mutually exclusive applications for initial licenses or construction permits are accepted for filing by the Commission and where the principal use of the spectrum will involve or is reasonably likely to involve the receipt by the licensee of compensation from subscribers in return for enabling those subscribers to receive or transmit communications signals.[22] In the *Second Report and Order* we concluded that PCS service would meet the criteria for auctionability.[23] Millin requests that we reverse that decision and conduct further inquiry concerning the possibility of non-subscription PCS.[24] We considered and rejected Millin's arguments in the *Fifth Report and Order* in this docket, stating that the overwhelming weight of the comments in that proceeding, as well as our experience with the PCS experiments that we have licensed, reflect that licensed PCS spectrum is likely to be used principally for the provision of service to subscribers for compensation.[25] We continue to believe that the record strongly supports the likelihood that PCS spectrum will be used principally for the provision of service to subscribers for compensation. Accordingly, we deny Millin's request.

III. AUCTION DESIGN AND PROCEDURES

A. Activity and Stopping Rules

12. Activity rules and stopping rules are intended to govern the speed and duration of bidding in an auction. An activity rule encourages each bidder to participate actively through the course of an auction. Activity rules are intended to ensure that simultaneous auctions with simultaneous stopping rules will close within a reasonable period of time and that bid prices will convey meaningful information during the course of the auction. In the *Second Report and Order,* the Commission adopted a three-stage Milgrom-Wilson activity rule as the preferred activity rule when a simultaneous stopping rule is employed.[26] Under this rule the auction moves from stage I to stage II when, in each of three consecutive rounds of bidding, the high bid has increased on less than some specified percent of the spectrum (measured in terms of MHz-pops) being auctioned.[27] The auction will move from stage II to stage III when in each of three consecutive rounds the high bid has increased on less than some specified percent of the spectrum (measured in terms of MHz-pops). The Commission, however, retained the flexibility to decide whether to use an activity rule, and if so what type of activity rule to use. We described possible activity rules, and stated the range of alternatives from which we would choose and the circumstances that might cause us to choose particular rules. We stated that we would announce the activity rule to be used by Public Notice before an auction.[28] A stopping rule specifies when an auction is over. In the *Second Report and Order* we stated that, for simultaneous auctions, our preferred stopping rule was that all markets would close simultaneously if a single round passed in which no new acceptable bids are submitted for any license. We retained the discretion, however, to announce at any point during a multiple round auction that the auction would end after a specified number of rounds.[29]

13. *Petitions.* Southwestern Bell Corporation (SBC), the GTE Service Corporation (GTE), and the Association of Independent Designated Entities (AIDE) argue that the three-stage Milgrom-Wilson activity rule is unnecessarily complex and should be simplified or eliminated.[30] SBC points out that the three-stage Milgrom-Wilson activity rule would require the Commission to track a large number of upfront payments and eligibility levels, and notes that the software the Commission intends to develop to track activity levels may not be developed in time. SBC states that allowing five automatic waivers, as the Commission proposes to do, does not reduce the uncertainty and expense which the activity rule imposes and may make bidding strategy more complex.[31] GTE states that the upfront payment formula, when combined with the activity rule, unnecessarily restricts bidder flexibility.[32] GTE states that the activity rules limit the ability of bidders to revise their plans in the course of the auction, particularly if information revealed during the latter stages of the auction causes a bidder to become interested in additional properties. The activity rules, according to GTE, discourage qualified entities from participating as fully as they might otherwise do, so that some licenses may not be awarded to the entity placing the highest value on them.[33] SBC urges the Commission to alter the stopping rule to allow the agency to issue a notice that bidding will close after a given number

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19 *Id.;*
20 Thumb Cellular Petition at 3-4.
21 *See Memorandum Opinion and Order* at ¶ ¶ 10-18.
22 47 U.S.C. § 309(j)(1).
23 *See Second Report and Order* at ¶ ¶ 55-56.
24 *See* petition of Millin Publications, Inc. (Millin).
25 *Fifth Report and Order* at n.8.
26 *Second Report and Order* at ¶ 144.
27 The number of "MHz-pops" is calculated by multiplying the population of the license service area by the amount of spectrum authorized by the license.
28 *Id.* at ¶ 133.
29 *Id.* at ¶ 132.
30 SBC Petition at 1-6; GTE Petition at 6-11; AIDE Petition at 12-13.
31 SBC Petition at 3-6.
32 GTE Petition at 7.
33 *Id.* at 9-10.

of rounds.[34] GTE and SBC ask the Commission to adopt a simpler activity rule, such as a requirement that bidders be active on a single license in each round.[35] AIDE urges that the activity rules be withdrawn, at least in the case of designated entities.[36] PacBell counters that the three-stage Milgrom-Wilson activity rule avoids delay, provides meaningful information, and allows bidders the flexibility to react to that information, and that software is available to help ensure that the Milgrom-Wilson rule will not be hard to implement.[37]

14. *Discussion.* As we noted in the *Second Report and Order,* the decision to use activity rules and the choice among activity rules involve tradeoffs among the speed of the auction, bidder flexibility, and simplicity.[38] The petitioners raise no issues relating to activity rules that we did not consider carefully in the *Second Report and Order.*[39] We see nothing in the petitions for reconsideration to cause us to change our opinion concerning the choices we made among these goals.

15. We do not believe that the Milgrom-Wilson activity rules will excessively restrict bidders' flexibility to bid for desired combinations of licenses or cause licenses to be awarded to bidders who value them less than other bidders. The rules were expressly designed to counteract the incentive to delay serious bidding that occurs in simultaneous auctions, without unduly limiting bidders' flexibility to pursue backup strategies and to use new information.[40] The restrictions placed on bidders at the beginning of the three-stage auction procedure are modest. In the first stage, to retain full eligibility a bidder need only bid on, or have the highest bid from the previous round on, licenses representing at least one-third of the MHz-pops he or she ultimately hopes to win. In the second stage, the bidder must bid on, or hold the high bid on, two-thirds of the MHz-pops he or she hopes to win. Only in the third stage are bidders required to bid on the full amount of MHz-pops they hope to acquire.[41] Bidders may shift bids among any combination of licenses from round to round.[42] Paul Milgrom points out that at the shift from stage I to stage II there will be no more than three bidders on an average license, and at the shift to stage III there will be at most bidders on an average license.[43] Because the progression to higher stages imparts such information, it gives the bidders important signals concerning the state of bidding. By stage III, bidding should be rapidly drawing to a close, and any major shifts in strategy should already have been implemented. Bidders who believe that they may want to expand their purchases if prices are unexpectedly low can guarantee their ability to do so by making a sufficiently high upfront payment.

16. In the *Second Report and Order,* we also stated our intention to reduce the complexity faced by bidders by developing bidding software and making it available to all bidders in auctions in which a Milgrom-Wilson activity rule is used.[44] SBC expresses concern that the software may not be available in time. Software was in fact developed in time for the July nationwide narrowband auction, and performed successfully in that auction. In light of that success, we have no doubt that appropriate software will also be available for the remaining narrowband and broadband auctions.

17. Finally, we remind petitioners that, in the *Second Report and Order,* we adopted the three-stage Milgrom-Wilson activity rules only as a preferred option.[45] We deferred to later, service-specific Orders the choice of actual rules to be used in auctions for individual services, depending, as discussed in the *Second Report and Order,* on the characteristics of the services and our experience with the conduct of auctions. In addition, we retained the flexibility to decide on an auction-by-auction basis, and to announce by Public Notice before the auction, whether to use an activity rule, and if so what type of rule.[46] Thus, if experience shows that the Milgrom-Wilson rules are unduly difficult to administer, we may shift to other activity rules, including the one recommended by petitioners requiring only that bidders be active on a single license in each round. We also expressly retained the discretion, requested by SBC, to announce at any point during a multiple round auction that the auction will end after some specified number of additional rounds.[47]

18. In the *Second Report and Order* the Commission also retained the ability to speed up an auction by announcing at any time during an auction that the next stage of the auction will begin in the next bidding round.[48] In this Order the Commission wishes to make explicit that this discretion could be exercised by employing an alternative rule for moving from one stage of the auction to the next. The Commission will announce by Public Notice prior to an auction its intent to use an alternative rule. One possible alternative rule would be that the auction will move to the next stage if in each of some fixed number of rounds, bidding activity is below some level measured as the ratio of new bids (measured in terms of MHz-pops) to available licenses (measured in terms of MHz-pops). The ratio of new bids to licenses may be a better measure of bidding activity than the percentage of total licenses on which the high bid has increased (measured in terms of MHz-pops) because it accounts for the possibility that bidding may be concentrated on a few licenses. In contrast, the latter measure indicates the same level of bidding activity regardless of how many bids are made on a given set of licenses.

B. Suggested Opening Bid

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[34] SBC Petition at 5.
[35] GTE Petition at 10-11; SBC Petition at 5.
[36] AIDE Petition at 12-13.
[37] PacBell Opposition at ii.
[38] *Second Report and Order* at ¶ 134.
[39] For instance, GTE notes that a bidder may be interested in some properties only if it can also acquire other key properties. GTE states that "under the modified Milgrom-Wilson rule, the bidder could be forced to choose between dropping out of the auction prematurely or staying active in markets that may prove to be less valuable if the bidder loses out in the other key markets." GTE Petition at 9-10. The *Second Report and Order* considers the same situation of interdependency and concludes that a bidder would have more flexibility with the three-stage Milgrom-Wilson rule than with another possible activity rule, that of starting the bidding with the third stage of the Milgrom-Wilson rule. *See Second Report and Order* at ¶ 142.
[40] *Id.*
[41] *Id.* at ¶ 137.
[42] *Id.* at ¶ 136.
[43] *Ex parte* submission of Paul Milgrom, June 21, 1994 at 2.
[44] *Second Report and Order* at ¶ 143.
[45] *Second Report and Order* at ¶ 144.
[46] *Id.* at ¶ 133.
[47] *Id.* at ¶ 132.
[48] *Id.* at n.110.

19. In the *Second Report and Order*, we stated that in multiple round auctions the Commission will generally specify minimum bid increments to speed the progress of the auction.[49] The bid increment is the amount or percentage by which the bid must be raised above the previous round's high bid in order to be accepted as a valid bid in the current round. We retained the discretion to use a "suggested" minimum bid increment rather than a required bid increment.[50]

20. In the recent nationwide narrowband auctions, it became apparent that the Commission may need further tools to avoid unnecessarily long auctions. In order to expedite the auction process further, we also reserve the discretion to establish a suggested opening bid on each license in addition to the minimum bid increment.[51] Where we adopt a suggested opening bid, initial bids will have to be above the minimum bid increment but may be below the suggested opening bid. Generally, we will establish suggested opening bids in the range of $.03 - $.20 per pop per MHz for each license. This suggested opening bid will provide bidders with an incentive to start bidding at a substantial portion of the license value, thus ensuring a rapid conclusion of the auction.

C. Commission Discretion During Auctions

21. In the *Second Report and Order*, as discussed *supra*, we chose our primary auction methodology, but noted that no one auction design is optimal for all auctionable services. We stated that we would adopt auction rules for specific services in subsequent Report and Orders, based on criteria established in the *Second Report and Order*. We further stated that when we announced individual auctions for specific services, we would specify more detailed procedures for those auctions in a Public Notice, but that those procedures also would be governed by criteria set forth in the *Second Report and Order*.[52] Our rules also afforded flexibility with respect to some auction procedures, such as those governing the duration of bidding rounds, minimum bid amounts, and stopping rules, and we stated that we might make decisions regarding such matters during the course of an auction.[53]

22. *Petition*. The National Association of Business and Educational Radio, Inc. ("NABER") asserts that the auction rules do not comply with the public interest and the Administrative Procedure Act[54] because they allow the Commission to circumvent the normal notice and comment procedure, and that the rules prevent providers of service from devising a business plan and auction strategy in advance.[55] NABER states that the Commission should eliminate its discretion to change the auction rules or procedures during a particular auction, that bidders need to know the rules which will apply for a particular service auction, and that interested parties should have the opportunity to provide meaningful comment before the final auction rules for particular services and frequencies are set.[56] NABER asserts that should the Commission change bidding methods in mid-stream without prior public comment, the Commission would violate the notice and comment rulemaking requirements of the Administrative Procedure Act, by its failure to keep a record and analyze and consider all relevant matter regarding those new rules.[57]

23. *Discussion*. We believe that the process we have used to adopt auction designs and implementation procedures and the rules themselves fully comply with the Administrative Procedure Act. In the NPRM in this docket, we provided notice of the auction designs we were considering and requested comment on issues of auction design and procedure. We received voluminous public comment on these issues. In the *Second Report and Order*, we carefully considered all comments and suggestions concerning a wide variety of proposed auction designs, including the comments and proposals of numerous experts in auction theory. We have established a broad framework for the conduct of license auctions, specifying a menu of auction designs and procedures from which we will choose for individual auctions. We have identified our preferred options, and have discussed the circumstances in which we believe the various options will be most appropriate in order to serve our statutory goals, and which are therefore most likely to be chosen. After the *Second Report and Order* was issued, we made, in addition, more specific choices of auction designs for particular services in Orders dealing with those services.[58] We have also established application, payment, and penalty procedures for individual services.[59] The procedures, we believe, afforded members of the public all of the procedural rights to which they are entitled under the Administrative Procedure Act.

24. Our rules, however, must also be flexible enough so that we can adjust our procedures to fit the circumstances of individual auctions. We will not know until we have gained some experience with simultaneous multiple round auctions exactly what values of such parameters as bidding increments and triggers for movement to the next auction phase work best under what circumstances. Consequently, we believe that it is important for those running the auctions to be able to use information generated in the early auctions and in the early rounds of individual auctions. Further, it may be important to be able to respond to the behavior of bidders in the course of particular auctions. We may find it desirable to allow more time for consultation between bidding rounds in complex auctions, for instance, or, in light of the statutory requirement to issue licenses expeditiously, to increase the bidding increment to hasten the conclusion of an auction if the auction is proceeding slowly. Clearly, notice and comment procedures would be unworkable in such cases. The flexibility that our rules permit us is analogous to the *ad hoc* decisional authority that may be exercised within other types of li-

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[49] *Second Report and Order* at ¶ 124.

[50] Under a suggested minimum bid increment rule, the auction would close if no bids or only one bid was submitted that was above the minimum bid increment. *Id.* at n.102.

[51] *See ex parte* submission of Paul Milgrom, May 19, 1994.

[52] *Id.* at ¶ 68.

[53] *Id.* at ¶ ¶ 123, 126, 132.

[54] *See* Administrative Procedure Act, 5 U.S.C. §§ 551 *et seq.*

[55] NABER Petition at 2.

[56] *Id.* at 8.

[57] *Id.* at 9; *see* 5 U.S.C. § 553.

[58] *See Third Report and Order* at ¶ ¶ 16-40, *Fourth Report and Order* at ¶ 11-18, and *Fifth Report and Order* at ¶ ¶ 27-57.

[59] *See Third Report and Order* at ¶ ¶ 41-60, *Fourth Report and Order* at ¶ ¶ 19-29, and *Fifth Report and Order* at ¶ ¶ 58-92.

censing proceedings, and our discretion here is similarly constrained by the general framework and standards embodied in our rules. The latitude remaining to the Commission to alter auction procedures is, however, necessary to ensure that we can make improvements as we become aware of the need for them, and that we can manage auctions efficiently. The Commission will exercise its discretion in a manner consistent with our clearly articulated goals and the general procedures we have established.

25. We have also taken care to safeguard bidders' interests. During the course of an auction only minor adjustments in procedures are permitted that will necessitate no major changes of strategy on their part. Further, we have stated clearly which procedures are, and which are not, subject to change during the course of an auction, so that bidders will know what kinds of changes to expect and to prepare for. We have stated that when we announce auctions for a particular services by public notice, we will also announce the procedures to be used in those auctions.[60] We believe that this approach will provide prospective bidders with ample information to plan rational bidding strategies.

26. Finally, although the Commission has never before used auctions as a licensing method, we note that our auction procedures afford as much, or more, detailed guidance to bidders than is usually provided in advance of an auction. For example, in conventional oral auctions the auctioneer customarily has the discretion to alter bid increments and other procedures at will in any manner and at any time during an auction. As in other types of auctions, we believe that it will be critically important to the success of our auctions to leave the Commission some discretion to fine-tune auction procedures between auctions and, in some cases, on an *ad hoc* basis, during the course of an auction. Accordingly, we affirm our original decisions to adopt rules that afford the Commission some flexibility to modify its procedures during the course of an auction, within the scope of the options we have delineated and under the circumstances described above.

D. Treatment of Upfront Payments

27. In the *Second Report and Order* we required bidders to tender a substantial payment in advance of the auction in order to deter frivolous or insincere bidding.[61] Upfront payments were also intended to provide a source of funds for collection of penalties for bid withdrawal.[62] The amount of the upfront payment was related to the level of eligibility the bidder wished to establish, measured in terms of the population and amount of spectrum encompassed by the licenses on which the bidder was permitted to bid. In some cases the upfront payment could amount to millions of dollars.[63] We required that upfront payments be submitted prior to bidding, and we did not permit use of letters of credit or Treasury bills for upfront deposits due to administrative difficulties in accepting payment in such forms, at least until the Commission has more experience in conducting auctions.[64] We stated that upfront payments made by a winning bidder would be applied to satisfy its down payment obligations, and that losing bidders' upfront payments would be returned if they wished to withdraw from further bidding.[65]

28. *Petitions.* GTE asserts that the Commission should adopt an interest-bearing evergreen deposit procedure for upfront deposits.[66] GTE states that, since the Commission is not currently authorized to establish interest-bearing accounts, substantial sums of money could be tied up in upfront deposits without any accrual of interest for substantial periods of time. GTE asserts that maximum bidder flexibility can be achieved by allowing bidders to add or withdraw deposit funds during the course of the auction. GTE states that the Commission needs to ensure that it has the requisite authority to permit the accumulation and payment of interest.

29. AIDE states that when a winning bidder's upfront payments, less bid withdrawal penalties, exceed the required deposit, the excess upfront payment should remain available for crediting to another auction or for refund to the winning bidder.[67] AIDE points out that, in the case of designated entities, the required deposit is only 10 percent. AIDE notes that the Commission has stated that it will apply this policy for losing bidders, and as a matter of equal protection the Commission should apply the same policy to winning bidders with excess upfront payments.[68]

30. AIDE requests clarification of footnote 133 in the *Second Report and Order*.[69] Footnote 133 reads:

> For example, an entity that is interested in bidding on several 30 MHz PCS licenses with a goal of providing service to a population of at most 50 million should make an upfront payment of $30 million ($.02 x 30 MHz x 50,000,000). That bidder will not be permitted to bid (at any time) in the auction, or be permitted to win, 30 MHz licenses covering more than 50 million pops.

31. *Discussion.* Allowing bidders to add funds to upfront deposits in order to increase their eligibility level, or to withdraw funds from upfront deposits, as GTE recommends, would add greatly to the complexity of the Commission's administrative task. The Commission would have to keep track of changes in eligibility due to changes in upfront payments, as well as to changes in bidders' activity levels, and would have to ascertain that fund transfers had taken place before permitting bidders to bid at the levels to which the additional payments entitled them. Because of the short intervals between bidding rounds, delays in the transfer of funds would likely create problems for both bidders and the Commission. For these reasons, we believe it is prudent to require bidders to submit upfront payments that represent the maximum level of bidding that they anticipate before the beginning of the auction. Bidders can always ensure that they will be able to expand their bid-

60 *Second Report and Order* at ¶ 68.
61 *Second Report and Order* at ¶ 171.
62 *Id.* at ¶ 176.
63 *Id.* at ¶ ¶ 172, 173.
64 *Id.* at ¶ ¶ 182, 184, 185.
65 *Id.* at ¶ 187, n.140.
66 GTE Petition at 11-13.
67 AIDE Petition at 15.
68 *Id.* at 16.
69 *Id.* at 13.

ding above their originally anticipated level by submitting a sufficiently large upfront payment and maintaining a high activity level.

32. We agree with AIDE that winners' upfront deposits, in excess of their required down payment deposits and any penalties they may owe, should be refunded expeditiously. We intend to refund excess upfront deposits of all bidders as soon as possible. We will not apply excess upfront deposit balances to subsequent auctions, however, due to the additional administrative difficulty of tracking the funds.

33. With respect to AIDE's request for clarification, we clarify that footnote 133 means that in any round of the auction, a bidder who has made an upfront payment of $30 million may bid on, or hold the high bid from the previous round on, 30 MHz licenses in markets with a combined population totaling not more than 50 million. The specific licenses on which the bidder submits bids may vary from round to round, but the total MHz-pop ceiling cannot be exceeded in any single round.

E. Default Penalty

34. In the *Second Report and Order* the Commission imposed a default penalty for withdrawing a bid after a simultaneous multiple round auction has closed.[70] This default penalty was set at 3 percent of the amount of the winning bid the next time the license is offered by the Commission, or 3 percent of the amount of the defaulting bidder's bid, whichever is less. The default penalty would be imposed in addition to the bid withdrawal penalty, which was set at the difference between the amount bid and the amount of the subsequent winning bid. We stated that the default penalty was intended to provide an incentive for bidders who wished to withdraw their bids to do so before the close of the auction. We stated that such a penalty was appropriate because a withdrawal that occurs after an auction closes is likely to be more harmful than one that occurs before closing. We stated that if a withdrawal occurs after the auction closes, other bidders will have little opportunity to revise their strategies, and the likelihood will be lower that the licenses will be awarded to those who value them most. We also stated that default imposes on the government the extra costs of re-auctioning the license.

35. *Petition.* AIDE asserts that the default penalty will produce a windfall to the Treasury if the winning bid exceeds the defaulting bid by more than 3 percent.[71] AIDE states that the defaulting bidder should pay no penalty if the second bid exceeds the defaulting bid by 3 percent or more, and that if the second bid exceeds the defaulting bid by less than 3 percent, the defaulting bidder's penalty should be the difference between the second winning bid and 103 percent of the defaulting bid.

36. *Discussion.* We believe that it is appropriate to charge the full 3 percent default penalty in addition to the bid withdrawal penalty whether or not the winning bid in the second auction exceeds the defaulting bid. As we stated in the *Second Report and Order,* the function of the default penalty is to encourage bidders who plan to withdraw their bids to do so before the close of the auction.[72] The additional costs to the Commission and to other bidders of auctioning the license a second time, and the increased likelihood that the license will not be won by the bidder who values it most, are incurred as a consequence of default regardless of the level of the bids. Even if the winning bid is higher than the defaulting bid, we have no reason to believe that it is higher than the winning bid would have been had the defaulting bidder withdrawn before the close of the auction, nor have we reason to believe that a high winning bid compensates for the undesirable effects of default. Consequently, we retain the default penalty as set forth in the *Second Report and Order.*

F. Disclosure of Bidding Information

37. In the *Second Report and Order* the Commission recognized the informational benefits to be gained from releasing bidder identities during an auction, but concluded that such information should not be released because "the risk of collusion and strategic manipulation outweighs the benefits of the additional information." Instead the Commission adopted an intermediate approach pursuant to which the bidder identification numbers and bid amounts for each bidder will be released at the end of each round of bidding. This approach provides bidders with useful information without incurring excessive risks of collusion and strategic manipulation.[73]

38. *Petitions.* GTE and Southwestern Bell request that the identities of bidders be released during the course of the auction. GTE requests that the identity of the bidder associated with each bidder identification number be disclosed during the bidding process.[74] SBC states that the Commission should announce both the identity of the highest bidder and the bid amount for each round of the auction.[75] GTE argues that a bidder must construct a strategy based on its own valuation of the spectrum as well as estimates of its competitors' valuations and past bids, and that a fundamental component of this exercise is knowledge of who the competitors are. GTE notes that the Commission's sole justification for not furnishing information about the identity of bidders is a concern for collusion, and states that the *Second Report and Order* includes other mechanisms for minimizing collusion. GTE states that increases in available information raise the level of competition and the efficiency of license assignments, and that access to bidder identification information may increase revenue from the auction process while ensuring award to the bidder who most highly values the license.[76] SBC argues that the decision to keep winning bidder identities secret creates an opportunity for collusive behavior because cartels could coordinate activities and punish violators without detection. SBC notes that if the identity of all bidders is known, the Commission and bidders need not be concerned with protecting bidders' identity. SBC states that knowing who the successful bidders are affects other bidders' ability to assess the accuracy of their valuation of the spectrum and allows them to ascertain that an aggregation of licenses is underway which might pose a competitive

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70 *Second Report and Order* at ¶ 154.
71 AIDE Petition at 14.
72 *Second Report and Order* at ¶ 154.
73 *Id.* at ¶ 158.
74 GTE Petition at 4-6.
75 SBC Petition at 8-10.
76 GTE Petition at 5-6.

threat. MCI states that because of the potential for bidder collusion and strategic manipulation, bidder identities should not be revealed.[77]

39. *Discussion.* Arguments in favor of disclosing bidder identities primarily turn on the value of the information in improving the quality of bids. Some auction experts argue that bidders' estimates of license values can be improved by comparing them to the valuations of their competitors.[78] Bidders' valuations of licenses may also be highly dependent on knowing the identity of neighboring carriers, especially regional leaders and competitors, and on knowing the manner in which complementary licenses are likely to be used and the compatibility of standards both inside and outside their desired service areas. Maximizing information available to bidders may increase bids by decreasing bidders' incentives to reduce their bids to avoid the "winner's curse," the tendency for the bidder who most overestimates the value of the item for sale to win an auction. Revealing bidder identities may facilitate awarding licenses to those who value them most highly by providing more information to bidders. More accurate valuation of licenses by bidders can thus improve the efficiency of license assignments. In addition, publicly disclosing the identity of other bidders may encourage vigorous bidding for licenses. Releasing bidder identities may increase interest in and media coverage of the auctions.

40. Our experience with the first narrowband PCS auction showed that preventing bidder identities from being revealed can be extremely difficult. In addition, if some but not all bidders know other bidders' identities, those bidders have an advantage in the quality of information available to them and in the potential ability to thwart others' bidding strategies. Concealing bidder identities may give an advantage to larger bidders that have the resources to devote to discovering other bidders' identities.

41. As we noted in the *Second Report and Order,* however, releasing the identities of high bidders may foster strategic manipulation, such as bidding up the prices of licenses needed by rivals, and may facilitate collusion.[79] Some auction experts argue that anonymity makes it harder to target a firm for strategic hold-up because the bidding and aggregation strategies of specific competitors cannot be easily detected.[80] Concealing bidder identities makes initiating collusive arrangements during the course of an auction more difficult because bidders will not easily be able to identify the parties against whom they are bidding, unless those parties voluntarily reveal their identities. On the other hand, concealing bidders' identities may not be critical to preventing collusion during an auction; existing antitrust laws and the FCC's collusion rules should be adequate to prevent collusive conduct. In any event, under an anonymous bidding scenario, if bidders want to collude they can simply disclose their bidder identification numbers to one another before the auction.

42. Because of the advantages of providing more information to bidders and the difficulties involved in ensuring that bidder identities remain confidential, we will generally release the identities of bidders before each auction. However, we recognize that experts disagree on the potential for knowledge of bidders' identities to facilitate collusion and other strategic behavior. Consequently we wish to have the flexibility to conceal bidder identities if further experience shows that it would be feasible and desirable to do so. We may also wish to test the effects of releasing identities of bidders. Consequently we are reserving the option to withhold bidder identities on an auction-by-auction basis. If we decide to withhold bidder identities for a particular auction, we will announce that decision by a service-specific auction Order. We will announce by Public Notice prior to each auction whether the identities of bidders will be made public in that auction.

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[77] MCI Comments at 3.

[78] *See e.g.* comments of PacBell on NPRM, Attachment by Paul R. Milgrom and Robert B. Wilson at 21.

[79] *Second Report and Order* at ¶ 158.

[80] Comments of NYNEX on NPRM, attachment by Robert G. Harris and Michael L. Katz, "A Public Interest Assessment of Spectrum Auctions for Wireless Telecommunications Services" at 9.

G. Standby Queue

43. *Petition.* GTE states that for 10 MHz blocks in broadband PCS the Commission should adopt the "standby queue" bidding mechanism considered in experiments sponsored by the National Telecommunications and Information Administration and conducted at the California Institute of Technology.[81] The standby queue allows parties seeking individual licenses to coordinate their bids in order to beat a bid for a combination of licenses. GTE asserts that the standby queue would allow bidders seeking to combine smaller blocks into a larger set of frequencies, or to combine blocks on a geographic basis, to obtain information about the status of bidding that would permit them to bid rationally and efficiently.

44. *Discussion.* The standby queue is a mechanism to be used in conjunction with combinatorial auctions. In the *Fifth Report and Order* we concluded that the disadvantages of combinatorial bidding were likely to outweigh the advantages for auctions of broadband PCS licenses, and we adopted simultaneous multiple round bidding as our auction methodology for broadband PCS licenses. Nevertheless, we left open the option to use combinatorial auctions if simultaneous multiple round auctions do not result in efficient aggregation of licenses, and if there are significant advances in the development of combinatorial auctions.[82] Although we have no current plans to use combinatorial auctions, if in future we do adopt such an auction methodology we will consider the use of a standby queue mechanism.

H. Filing Fees

45. *Petition.* William E. Zimsky (Zimsky) states that the rule imposing filing fees for the filing of short-form applications for auctions should be deleted.[83] Zimsky asserts that because there is no provision in 47 U.S.C. § 158(g) for imposing the filing fee for the new short-form application, the Commission lacks the statutory authority to impose such a fee. Zimsky also asserts that, even if the Commission has such statutory power, to impose a filing fee on all bidders is unreasonable because the filing fee was designed to recoup the costs of fully processing the application. Since only auction winners will submit long-form applications and have their applications scrutinized, the losing bidders do not receive this service. Consequently, the Commission's proposed scheme is unconstitutional, he argues, because a user fee which is not reasonably related to, or a fair approximation of, the cost incurred by the government in providing the service for which the fee is assessed, effects a taking of applicants' property without just compensation, in violation of their fifth amendment rights. Zimsky cites *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 163 (1980); *United States v. Sperry Corp.*, 493 U.S. 52, 60 (1989) in support of his argument.

46. *Discussion.* The Commission has requested express statutory authority to impose section 8 application fees for short form applications. In the absence of such express authority, we do not currently impose fees for short-form applications. However, long-form applications in most services are subject to fees under section 8. Consequently we find Zimsky's petition to be moot, and we dismiss it.

I. Waiver Requests in Short-Form Applications

47. Cable & Wireless, Inc. (CWI) asks that the Commission reconsider its rules that appear to mandate dismissal of the short-form application, (Form 175) that do not certify compliance with the foreign ownership provision of Section 310 of the Communications Act, notwithstanding the filing of a request for waiver or other relief.[84] CWI asserts that the Commission should permit participation at auction where the applicant certifies to the pendency of such a waiver request. In considering the acceptance for filing of short-form applications, the Commission will accept certifications that state that a request for waiver or declaratory ruling concerning the requirements of section 310 is pending.[85]

J. Rules Prohibiting Collusion

48. In order to prevent collusion in bidding, the Commission in the *Second Report and Order* stated, ... bidders will be required to identify on their short-form applications any parties with whom they have entered into any consortium arrangements, joint ventures, partnerships or other agreements or understandings which relate in any way to the competitive bidding process. Bidders will also be required to certify on their short-form applications that they have not entered into any explicit or implicit agreements, arrangements or understandings of any kind with any parties, other than those identified, regarding the amount of their bid, bidding strategies or the particular properties on which they will or will not bid. . . . After such applications are filed and prior to the time that the winning bidder has made its required down payment, all bidders will be prohibited from cooperating, collaborating, discussing or disclosing in any manner the substance of their bids or bidding strategies with other bidders, unless such bidders are members of a bidding consortium or other joint bidding arrangement identified on the bidder's short form application.[86]

49. *Petition.* BET Holdings, Inc. (BET) states that the above requirements prevent bidders from entering into any new agreements, joint ventures or similar arrangements with other entities after filing a short-form application.[87] BET claims that as a consequence bidders may be locked into bidding arrangements significantly before the commencement of the auctions, and will be unable to modify their bidding strategies, consult with experts or others, or enter into additional alliances with new parties any time after the filing of the short-form application. BET states that the collusion rule is an unrealistic constraint on lawful business behavior. For example, according to BET, if a company does not identify affiliates or others with whom it must consult, the company would be forbidden from solic-

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[81] GTE Petition at 13-14.

[82] *Fifth Report and Order* at ¶ 35.

[83] *See* William E. Zimsky Petition.

[84] *See* petition of CWI.

[85] On January 5, 1994, CWI also filed a petition seeking a declaratory ruling that the public interest warrants grant of common carrier radio license applications to U.K. citizens and/or corporations that possess ownership interests in excess of the foreign ownership benchmarks in Section 310(b)(4) of the Communications Act. We expect to address the merits of this petition in a separate Declaratory Ruling.

[86] *Second Report and Order* at ¶ 225.

[87] BET Petition at 10.

iting research, sharing resources, or discussing its bids until after the winning bidder tenders its down payment.[88] BET requests that the Commission rely on antitrust law as a safeguard against collusion.

50. *Discussion.* While we intend to rely primarily on the antitrust laws to prevent bidding collusion, we believe that the anticollusion rules in the *Second Report and Order* will provide an important additional tool that will enable the Commission to detect, prevent, and punish collusion. To prevent and detect collusion, we believe that it is important to have clearly stated rules concerning the entities with whom communication about bidding strategies is permissible. The requirement that an entity identify at the time of the short-form application those affiliates, subsidiaries, or others with whom it has agreements concerning bidding, and the prohibition of communication concerning bidding with entities identified by other bidders, serve this purpose and are not particularly burdensome. Similarly, prohibiting additional agreements and alliances concerning bidding between applicants bidding for the same licenses, after applications have been filed and the identities of all applicants are known, seems a prudent deterrent to collusion that should have only a minimal and temporary effect on bidders' flexibility. We wish to make explicit our intention that the prohibition extend to post-application settlement agreements and discussions concerning settlement agreements.

51. We do believe, however, that our prohibition on communication among bidders and formation of agreements among bidders after applications have been filed may have been excessively broad in that it includes communications and agreements with bidders who are not bidding against each other, and so may prevent useful agreements that have no effect on the competitiveness of bidding. Consequently, we are modifying our collusion rules, which currently prohibit bidders from communicating with one another after short-form applications have been filed regarding the substance of their bids or bidding strategies and which also prohibit bidders from entering into consortium arrangements or joint bidding agreements of any kind after the deadline for short-form applications has passed. In order to permit certain bidders to respond to higher than expected license prices by combining their resources during an auction, we will now permit bidders who have not filed Form 175 applications for any of the same licenses to engage in discussions and enter into bidding consortia or joint bidding arrangments during the course of an auction. We conclude that where bidders have not applied for any of the same licenses there is little risk of anticompetitive conduct and therefore we believe that it is appropriate to relax our collusion rules to permit bidders in this context to have greater flexibility to increase their competitveness in the auction by combining their resources, provided that no change of control of any applicant takes place.

52. In addition, we now believe that entering into consortium arrangements or adding equity partners during an auction may have a useful effect in enabling bidders to acquire the capital necessary to bid successfully for licenses. We have concluded that formation of consortia or changes in ownership after the filing of short-form applications will not necessarily have anticompetitive effects, provided they do not involve parties that might have bid against each other and do not result in a change in control of the applicant. Consequently, we wish to modify our rules regarding amendments to short-form applications. As a result of our experience in the nationwide narrowband PCS auction, we believe that it is necessary to allow applicants to amend their FCC Form 175 applications to make ownership changes after the filing deadline has passed, provided such changes do not result in a change in control of the applicant. Permitting such amendments will provide bidders with flexibility to seek additional capital after applications have been filed, while ensuring that the real party in interest does not change. Accordingly, we will modify Section 1.2105(c) to permit applicants to amend their FCC Form 175 applications to reflect ownership changes that do not result in a change in control of the applicant, provided the parties have not filed Form 175 applications for any of the same licenses. Such changes shall not be regarded as major amendments to an application, provided they do not result in a transfer of control of the license or the applicant and do not change control of the company.

53. Situations may arise in which an applicant has some common ownership interest with another bidder. We wish to clarify that, unless that other entity is expressly identified as an entity with whom the applicant has an agreement concerning bidding, we will prohibit communication concerning bidding with that bidder, as described in the *Second Report and Order,* even if the other bidder is identified on the applicant's short-form application as having some common ownership interest with the applicant. We will retain the anticollusion rules as set forth in the *Second Report and Order,* with these clarifications.

K. Information Disclosure by Applicants and Licensees

54. *Petitions.* Two petitions deal with the amount of information auction participants are required to disclose. GTE requests that the Commission require applicants to provide full ownership disclosure in their short-form applications.[89] GTE asserts that by enabling the Commission and competing applicants to assess the legitimacy of auction applicants, full disclosure facilitates the award of licenses to qualified and eligible service providers. According to GTE, full disclosure also promotes open and informed bidding decisions.

55. SBC asks that the Commission minimize requirements for disclosure of information upon transfer of licenses.[90] SBC states that the point of transfer disclosures is to "'prevent unjust enrichment as a result of the methods employed to issue licenses and permits.'"[91] SBC asserts that rules designed to prevent unjust enrichment should be solely applicable, if at all, to designated entities that receive special accommodations, since the risk of unjust enrichment is high only in auctions where such special accommodations are provided. SBC asserts that the formation of reasonable and efficient alliances would be discouraged by the mandate to expose the details of the alliance to competitors. SBC particularly objects to the requirement that

[88] *Id.* at 11.
[89] GTE Petition at 2-4.
[90] SBC Petition at 6-8.
[91] *Id.* at 6 (*citing* 47 U.S.C. §309(j)(4)(E)).

any management agreements or consulting contracts be filed. SBC seeks clarification that the disclosure requirements will apply only to the licensees which either have not begun to offer service or have only offered service for some minimal period of time.

56. *Discussion.* With respect to ownership disclosure in short-form applications, in the *Second Report and Order* we decided to require applicants to furnish only minimal information in short-form applications and bidder certifications prior to auctions in order to reduce administrative burdens and minimize the potential for delay.[92] Further ownership disclosure requirements, however, were adopted on a service-specific basis in later Reports and Orders.[93] We believe that GTE's concerns are fully met by these requirements.

57. As for transfer disclosure requirements, Congress in the Budget Act required us to develop and test alternative auction designs.[94] We noted in the *Second Report and Order* that in addition to allowing detection of unjust enrichment, transfer disclosure requirements would provide data necessary for evaluation of our auction designs.[95] We noted that the reporting requirements would allow us to monitor our compliance with the Congressional directive in Section 309(j)(3)(B) to ensure that "new and innovative technologies are readily accessible to the American people by avoiding excessive concentration of licenses and by disseminating licenses among a wide variety of applicants. . . ."[96] The information will be useful in meeting our statutory obligation to report to Congress on the outcome of the auctions.[97] The information we acquire from transfer disclosures, including purchase price and other aspects of the sale contracts and management agreements, will enable us to determine the ultimate distribution of licenses and the value of the spectrum for particular uses, and will permit comparisons between licenses awarded with and without designated entity provisions. Such analyses require collection of data from all licensees, not just from designated entities or those who have not begun to offer service or have only offered service for a short period of time. As we stated in the *Second Report and Order,* we do not expect the transfer disclosure requirements to be burdensome to licensees because the documents to be submitted will have been prepared for other purposes in any event. Moreover, parties may request confidential treatment of competitively sensitive information pursuant to Sections 0.457 and 0.459 of our Rules.[98] Consequently we will retain transfer disclosure requirements for all transfers of licenses obtained by competitive bidding.

L. Application-Processing Rules

58. In the *NPRM* in this proceeding the Commission stated:

In order to avoid needless duplication, we propose that the following general filing and processing rules apply to all PCS: Sections 22.3-22.45 and 22.917(f), and 22.918-22.945, 47 C.F.R §§ 22.3-22.45, 22.917(f), and 22.918-22.945. For those PCS applicants who file on Form 574, we believe that Sections 90.113-90.159 of our rules, 47 CFR §§ 90.113-90.159, could be used to process those applications with appropriate modifications.[99]

59. *Petition.* AIDE asserts that the Commission acted improperly in proposing substantive PCS application-processing rules in the *NPRM* because, it argues, such rules are outside the scope of this rulemaking, which is limited to implementation of the competitive bidding requirements of §309(j) of the Communications Act.[100] AIDE argues that the Commission's proposal of application-processing rules is legally insufficient to constitute a valid notice of proposed rules, and that some of the rules cited have no immediate applicability to PCS service. AIDE asserts that in the *Second Report and Order* the Commission failed to respond to the merits of the arguments concerning filing and processing rules in AIDE's comments on the *NPRM.* AIDE concludes that the Commission needs to issue a supplemental *Notice of Proposed Rulemaking* to adopt license-processing rules for PCS.

60. *Discussion.* The competitive bidding process is a means of assigning licenses, and rules and procedures for processing of license applications are an integral and necessary part of that process. The Commission adopted few filing or processing rules in the *Second Report and Order.* Those rules that the Commission did adopt pertaining to the filing and processing of applications and certifications were clearly proposed in the NPRM.[101] The rules to which AIDE refers were adopted not in the *Second Report and Order* but in subsequent Orders establishing auction rules for specific services.[102] We address AIDE's petition relating to those rules either in the Orders in which they were adopted or in reconsiderations of those Orders.[103]

M. Financial Qualifications

61. In the *Second Report and Order,* the Commission stated that applicants filing short- form applications would be required to certify that they are financially qualified pursuant to Section 308(b) of the Communications Act. The applicants would also be required to certify that they satisfy any financial qualification requirements for the service in question.[104]

62. *Petition.* AIDE states that applying competitive bidding and payment requirements in addition to existing financial qualification requirements disadvantages designated entities, who have historically been constrained by difficulties in capital formation and financing. AIDE recommends that short-form applications not require any certification of financial qualification. If an application

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92 *Second Report and Order* at ¶ 165.
93 *See Third Report and Order,* Appendix at 13; *Fifth Report and Order* at ¶ 62.
94 47 U.S.C. 309(j)(3).
95 *Second Report and Order* at ¶ 214.
96 *Id.* at ¶ 215.
97 *See* Budget Act, 47 U.S.C. § 309(j)(2).
98 *Second Report and Order* at ¶ 215, *citing* 47 CFR §§ 0.457, 0.459.
99 *NPRM* at ¶ 128.
100 AIDE Petition at 20-21.
101 *See Second Report and Order* at ¶ ¶ 164-168, *NPRM* at ¶ ¶ 96-101.
102 *See Third Report and Order* at ¶ 41, n.18; *Fifth Report and Order* at ¶ 83.
103 *See Fifth Report and Order* at ¶ 83.
104 *Second Report and Order* at ¶ 166.

became mutually exclusive, according to AIDE, the applicant's payment of its winning bid would demonstrate that it was financially qualified. If the application did not become mutually exclusive, then the applicant should have a short period in which to file any required demonstration of financial qualifications by amendment.[105]

63. *Discussion.* We believe that, in order to prevent the delay in bringing service to the public that might be occasioned by bankruptcies or by prolonged financial negotiations, it is important to require licensees to have the financial ability to construct and operate a system in addition to being able to purchase the license. Consequently we will continue to require applicants to certify on their short-form applications that they meet any existing financial qualification requirements of the services in which licenses are auctioned. We will not, however, impose additional showings of financial qualification as a part of the auction process.

IV. DESIGNATED ENTITIES

A. Introduction

64. Several provisions of the Budget Act address participation by small businesses, rural telephone companies, and businesses owned by women and minorities (referred to collectively as "designated entities") in the competitive bidding process and in the provision of spectrum-based services. Specifically, Section 309(j)(4)(D) of the Act, provides that, in prescribing competitive bidding regulations, the Commission shall, *inter alia*, ensure that small businesses, rural telephone companies, and businesses owned by members of minority groups and women are given the opportunity to participate in the provision of spectrum-based services, and, for such purposes, consider the use of tax certificates, bidding preferences, and other procedures . . .[106] In addition, section 309(j)(3)(B), provides that in establishing eligibility criteria and bidding methodologies the Commission shall seek to promote the objectives of "economic opportunity and competition and ensur[e] that new and innovative technologies are readily accessible to the American people by avoiding excessive concentration of licenses and by disseminating licenses among a wide variety of applicants, including small businesses, rural telephone companies, and businesses owned by members of minority groups and women." To promote these objectives, section 309(j)(4)(A) expressly states that the Commission is required "to consider . . . alternative payment schedules and methods of calculation, including lump sums or guaranteed installment payments, with or without royalty payments, or other schedules or methods."[107]

65. In the *Second Report and Order* we adopted a broad menu of provisions that the Commission might employ to implement these statutory provisions. We adopted general provisions and eligibility rules designed to ensure that small businesses, rural telephone companies, and businesses owned by members of minority groups and/or women were afforded the opportunity to participate in both the competitive bidding process and in the provision of spectrum-based services. Specifically, we provided that small businesses (including those owned by women and/or minorities and rural telephone companies) that are winning bidders for certain blocks of spectrum could pay in installments over the term of their licenses. We also indicated that rural telephone companies may be eligible for bidding credits for licenses obtained in their service areas if they make an additional infrastructure build-out commitment beyond any existing performance requirements. We indicated that bidding credits may be available to designated entities on certain frequency blocks. In addition, we retained the option of establishing set-aside spectrum incertain services, in which eligibility to bid may be limited to some or all designated entities. Finally, we stated that we would consider the use of tax certificates as a means of creating incentives both for designated entities to attract capital from non-controlling investors and to encourage licensees to assign licenses to designated entities in post-auction transactions.

66. In the *Second Report and Order* we recognized that the provisions applicable to particular designated entities would vary depending on the nature of each individual service. For example, we retained the discretion to modify our general designated entity provisions for capital intensive services such as broadband PCS. In this regard, we stated that we would evaluate on a service-specific basis the capital requirements and other characteristics of the service to determine the appropriate provisions. We continue to believe that it is essential for the Commission to retain flexibility to select, and if necessary to modify, the general designated entity provisions and eligibility requirements on a service-specific basis depending on the capital requirements and construction costs of the particular service.

B. Rural Telephone Company Definition

67. *Background.* In the *Second Report and Order,* we adopted a definition of "rural telephone company" that includes independently owned and operated local exchange carriers that (1) do not serve communities with more than 10,000 inhabitants in the licensed area, and (2) do not have more than 50,000 access lines, including all affiliates.[108] We stated our belief that a limitation on the size of eligible rural telephone companies was appropriate because Congress did not intend for us to provide special treatment to large LECs that happen to serve small rural communities.[109]

68. *Petitions.* Several parties filed petitions for reconsideration of the *Second Report and Order* requesting that we modify our standard definition for rural telephone com-

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[105] AIDE Petition at 19-20.

[106] 47 U.S.C. § 309(j)(4)(D).

[107] *See also* 47 U.S.C. § 309(j)(4)(C)(ii), requiring the Commission, when prescribing area designations and bandwidth assignments, to promote "economic opportunity for a wide variety of applicants, including small businesses, rural telephone companies, and businesses owned by members of minority groups and women"; section 309(j)(3)(A), establishing the objective to promote "the development and rapid deployment of new technologies, products, and services for the benefit of the public, including those residing in rural areas, without administrative or judicial delays"; section 309(j)(12)(D)(iv), requiring that the Commission's 1997 report to Congress evaluate, *inter alia,* whether and to what extent "small businesses, rural telephone companies, and businesses owned by members of minority groups and women were able to participate successfully in the competitive bidding process."

[108] 47 CFR § 1.2110(b)(3).

[109] *See Second Report and Order* at ¶28 2.

panies. Petitioners' proposals include requests that the Commission amend its definition of "rural telephone company" (1) to expressly include municipal- and government-owned telephone companies within the "rural telephone company" definition in accordance with the earlier Senate version of the Budget Act;[110] (2) to define "rural telephone company" as a local exchange carrier with annual revenues of less than $100 million or serving no more than 100,000 access lines;[111] and (3) to include within the definition of "independently owned and operated" LECs that either operate 50,000 access lines or less or serve communities of 10,000 or fewer inhabitants.[112]

69. In addition, Blooston, Mordkofsky, Jackson & Dickens (Blooston) and South Dakota Networks, Inc. (SDN) request that the Commission eliminate the term "independently owned and operated" from the definition of "rural telephone company." According to Blooston, this restriction is unnecessary to prevent the largest telephone companies from taking advantage of provisions provided for rural telephone companies, since this same purpose is already served by the 50,000 access line limit, Blooston argues the Commission should amend its eligibility rules to indicate that they include the access lines of affiliates. Similarly, SDN indicates that the Commission should include "and affiliates" after "50,000 or fewer access lines" in the current definition. SDN maintains that the current language penalizes holding companies structured to permit telephone companies to offer paging and other nonregulated services.

70. The National Telephone Cooperative Association (NTCA) requests that the Commission amend the definition of rural telephone company to include any local exchange carrier with annual revenues of less than $100 million or serving no more than 100,000 access lines. NTCA also indicates that the term "independently owned" should not exclude small rural telephone companies that are affiliated with each other and that rural telephone company consortia should be permitted. USIN similarly advocates a "rural telephone company" definition based annual revenues of less than $100,000,000 or less than 100,000 access lines. According to USIN a revenue-based test is more accurate than net worth/net profit test.

71. The Rural Cellular Association (RCA), South Dakota Network, Inc. (SDN) and NTCA ask that the Commission amend the definition of rural telephone companies to include any independently owned and operated local exchange carriers ("LECs") that *either* operate 50,000 access lines or less *or* serve communities of 10,000 or fewer inhabitants. According to NCTA and RCA, the existing definition needlessly excludes many small independent telephone companies that serve rural areas. SDN alternatively requests that we revise the definition to include carriers with 100,000 or fewer access lines or up to $100 million in annual revenues.

72. Finally, Anchorage Telephone Utility (ATU) requests that the Commission modify the definition of rural telephone companies to include government-owned telephone companies. According to ATU, such a modification is necessary to achieve congressional intent. ATU notes that the Senate bill included municipally-owned telephone companies in its definition of rural telephone companies. ATU's argues that the Senate Bill mandates special consideration for rural telephone companies and directed the FCC to grant "rural program licenses" to "qualified" common carriers and explicitly said that the category of "qualified" carriers included all state-owned and municipally-owned telephone companies.[113] As evidence Congress' intent to include these provisions in the enacted version of Budget Act, ATU asserts that the Conference Report declares that the Senate's "findings" are incorporated by reference.

73. *Oppositions and Replies.* In its Comment on Petitions for Reconsideration, BET supports retention of the Commission's existing generic rural telephone company definition.[114] BET maintains that adoption of RCA's proposal to define rural telephone companies as LECs that have 50,000 access or fewer or serve communities with no more than 10,000 inhabitants will allow large LECs that "happen to serve rural areas" to qualify for designated entity provisions. In response to BET's Comments, RCA asserts that the "independently owned and operated" requirement for rural telephone company eligibility will prevent large LECs from qualifying for rural telephone company provisions. RCA also restates its request for an amendment to the general rural telephone company definition to include LECs that serve 100,000 access lines or fewer.[115]

74. In light of the Commission's decision in *Fifth Report and Order* in this proceeding, which adopted an alternative rural telephone company definition, NTCA argues that the Commission should abandon its generic rural telephone company definition and instead establish rural telephone company eligibility criteria on a service-specific basis. Alternatively NTCA proposes that we define rural telephone companies to include LECs that have annual revenues not in excess of $125 million or that serve no more than 100,000 access lines.[116] Tri-County Telephone Company, Inc. (Tri-County) supports SDN's proposed rural telephone company definition (50,000 access lines *or* serves no community with more than 10,000 inhabitants or alternatively 100,000 access lines or less).[117]

75. *Discussion.* We are persuaded by petitioner's arguments that the current generic "rural telephone company" definition is overly restrictive and effectively excludes many independently owned telephone companies that serve rural areas.[118] In the *Fifth Report and Order* we departed from our generic definition of rural telephone companies in the context of broadband PCS by adopting a definition that includes any local exchange carrier having 100,000 or fewer access lines, including all affiliates.[119] In adopting this definition of a "rural telephone company," we sought to

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[110] *See* Anchorage Telephone Utility (ATU) Petition.

[111] *See* Petitions of The National Telephone Cooperative Association (NTCA), South Dakota Network, Inc. (SDN) and U.S. Intelco Networks, Inc. (USIN).

[112] *See* Petitions of the Rural Cellular Association (RCA) and SDN.

[113] *See* ATU Petition at 2-3.

[114] BET Comments at 2.

[115] RCA Reply at 2.

[116] NTCA Reply Comments at 4.

[117] Tri-County Reply at 3.

[118] *See* RCA Petition at 4-5; USIN Petition at 10; NTCA Petition at 2.

[119] *See Fifth Report and Order* at ¶ 198.

achieve the congressional goal of promoting the rapid deployment of service in rural areas by targeting only those telephone companies whose service territories are predominantly rural in nature, and who are thus likely to use their wireline telephone networks to build infrastructures to serve rural America.[120] For purposes of our rules governing broadband PCS licenses, we indicated our belief that this goal could best be achieved if we defined "rural telephone companies" as those local exchange carriers having 100,000 or fewer access lines, including all affiliates. We concluded that this definition included virtually all telephone companies whose service areas are predominantly rural.

76. For the foregoing reasons, we also believe that using the 100,000 access line definition as our standard rural telephone company definition will better serve our goals of encouraging the provision of service to rural areas than the definition previously adopted in the *Second Report and Order*. Accordingly, we will amend our standard definition of "rural telephone company" to include all local exchange carriers with 100,000 access lines or fewer, including affiliates. In general, we believe that this definition will more precisely capture those carriers that are truly rural in nature, while excluding the largest telephone carriers that do not face similar capital formation problems. We believe that this definition will also better achieve Congress' goal of fostering the development and rapid deployment of new technologies and services to rural areas by making special measures available to legitimate rural telephone companies that require such provisions in order to meaningfully participate in the provision of service to rural areas without giving such benefits to large companies that do not require such assistance. Rural telephone companies that satisfy this definition thus will be eligible for rural telephone company provisions in each service where such provisions are established.[121]

77. As indicated above, Blooston, SDN and NTCA request that we eliminate the phrase "independently owned and operated" from the definition of "rural telephone company." These petitioners assert that the "independently owned and operated" restriction in the rural telephone company definition was intended to prevent large telephone companies from taking advantage of rural telephone company benefits, but that this purpose is served by the access line limit. In this regard, SDN argues that such language unduly penalizes holding companies of nonregulated services and entities created by groups of telephone companies to provide equal access, SS7, and other services.

78. We agree. The new 100,000 access line rural telephone company definition adopted above, includes the access lines of affiliates. Under the affiliation rules established in the context of broadband PCS, and adopted below as our generic affiliation rules, the access lines of holding companies, parent companies or affiliates of rural telephone companies that are not independently owned will be attributed for purposes of determining eligibility. This definition will capture most of the independently owned rural telephone companies, while excluding carriers affiliated with the largest LECs. In addition, we are concerned that the requirement that a rural telephone company must be independently owned would unnecessarily exclude rural telephone companies that are part of a holding company structure. Therefore we will delete the "independently owned and operated" requirement from our standard rural telephone company definition.

79. With respect to ATU's request that we amend our definition of rural telephone company to include municipal and government owned telephone companies that are owned by governmental authorities, we do not believe that such a change is warranted. ATU contends that Congress meant to mandate special consideration not only for telephone carriers serving rural areas but also for all municipally-owned telephone companies, even those with wholly or predominantly urban service areas.[122] This argument is based on ATU's interpretation of the Senate bill which preceded the enacted Budget Act. ATU argues that the Senate bill containing the prototype of a mandate for special consideration for rural telephone companies directed the FCC to grant "rural program licenses" to "qualified" common carriers and explicitly said that the category of "qualified" carriers included all state-owned and municipally-owned telephone companies. ATU further states that the report of the conference committee that drafted the Budget Act declares that the Senate's "findings" are incorporated by reference.[123] ATU also asserts that without the aid of special assistance it and most other state-owned and municipal telephone companies will not be able to purchase spectrum licenses at auction because it is politically infeasible for them to generate and retain enough surplus revenue to fund such investments, due to popular aversion to increases in taxes or telephone rates.[124]

80. As we indicated in the *Fifth Report and Order*, we are not persuaded by ATU's arguments.[125] We can find no specific evidence that Congress intended the term "rural telephone companies" to include all state or municipally-owned telephone companies. In fact, the preceding bill contained an explicit mandate for preferential treatment of government-owned telephone companies that was deleted from the enacted bill. To the contrary, the fact that an antecedent bill contained an explicit mandate for preferential treatment of government-owned telephone companies that was deleted from the enacted bill could just as easily be interpreted as an indication that Congress rejected such a rule. We also disagree that state and municipal governments are without the means to participate successfully in auctions. As we noted in *Fifth Report and Order* such governments have substantial capabilities to raise funds through private financing, bond offerings and taxation.[126]

C. Rural Telephone Company Consortia

[120] We also note that the unique technological requirements and the capital intensive nature of broadband PCS dictated that we adopt this definition of "rural telephone company."

[121] Such companies also will be eligible for special treatment under our cellular attribution rules for broadband PCS. *See* 47 CFR § 24.204(d)(2)(ii).

[122] ATU Petition at 2-3.

[123] *Id.*

[124] *Id.* at 4-5.

[125] *See Fifth Report and Order* at ¶203.

[126] *See Fifth Report and Order* at ¶ 200. In any event, most state and municipally owned telephone systems (although not ATU) will be captured by our new 100,000 access line rural telephone company definition.

81. *Petitions.* Telephone and Data Systems, Inc. (TDS) requests that the Commission relax the eligibility requirements for rural telephone company bidding consortia by (1) eliminating the 50,000 access line limit for rural telephone company consortium applicants; (2) allowing companies with more than 50,000 access lines, directly or through affiliates, to participate in rural telephone company consortia by demonstrating that more than 50 percent of their access lines company-wide (including affiliates) and over 50 percent of those in the proposed service area serve only communities with 10,000 or fewer inhabitants and (3) providing that all rural telephone companies in consortia with 50,000 access lines or less have the right to hold up to 60 percent of the equity in the consortium. SDN and NTCA also argue that the Commission should allow rural telephone companies to form consortia, since combining telephone companies would not alter their rural nature, so long as the rural telephone company retains at least 50.1 percent equity and control.

82. USIN similarly requests that small businesses, including rural telephone companies, be allowed to qualify for special provisions if they pool their resources into consortia, provided such consortia are controlled by designated entities. According to USIN, if such consortia are not permitted, rural telephone companies and other small businesses may be foreclosed from participation in the auction process and in the provision of auctionable services. USIN also indicates that efficiencies and economies of scale are created by aggregation and thus special measures should be provided to these entities who may be able to provide service most efficiently.

83. *Discussion.* We deny the requests of TDS, SDN,[127] and NTCA that we modify the standard definition of rural telephone company to eliminate or relax the access line limit for rural telephone company consortia. In the *Second Report and Order* as a general matter, we declined to provide exceptions to our designated entity eligibility criteria for applicants that are consortia of various individual entities, which in combination fail to qualify as designated entities.[128] We found that such combinations, if they deviate from our standard definitions of designated entities, should not be eligible for provisions expressly designed for designated entities. This conclusion was based on our desire to provide economic opportunity to those entities designated in the statute and to ensure such entities the opportunity to provide spectrum-based services. We concluded that establishing exceptions to our definitions for consortia (even those wholly comprised of otherwise qualified designated entities) would undermine this objective by diluting the economic opportunity for individual qualified designated entities. We also found that allowing applicants to be formed from a combination of eligible and ineligible entities would invite attempts to abuse the designated entity provisions by those not entitled to them.

84. However, in the *Second Report and Order* we noted that we may determine on a service-specific basis to allow a designated entity consortium to receive other benefits based on equity and operational participation in the consortium by one or more designated entities. We retained the flexibility to enable designated entity consortia to qualify for special provisions particularly where the capital costs of a particular service are high and the formation of consortia is thus essential to foster investment in designated entity ventures and to enable such entities to compete in the provision of such service. In this regard, in the *Fifth Report and Order* we allowed consortia comprised of small businesses to qualify for all of the measures applicable to individual small businesses provided each member of the consortium individually satisfies the definition of a small business. We found that given the "exceptionally large capital requirements" associated with broadband PCS, allowing small businesses to pool their resources in this manner was necessary to help them overcome capital formation problems and thereby ensure their opportunity to participate in auctions and to become strong broadband PCS competitors.

85. As a general matter, we will continue to determine whether to permit designated entities to receive benefits based on their participation in consortia on a service-specific basis, depending on the capital requirements and other characteristics of the particular service. We modify the *Second Report and Order,* however, to provide that consortia may be permitted to qualify for any designated entity provisions (where each member individually meets the eligibility requirements) on a service-specific basis, where the capital requirements of the service are high. Where, as in broadband PCS, we find that the capital requirements necessitate allowing designated entities to pool their resources to help them overcome capital formation problems and thereby ensure their opportunity to participate in auctions and in the provision of service, we may adopt rules allowing such consortia to qualify for designated entity provisions.

D. Affiliation Rules

86. *Petitions.* Blooston and NTCA request that the Commission clarify the meaning of "affiliate" for purposes of access line aggregation. According to Blooston, passive investments by a rural telephone holding company in other telephone companies should not preclude eligibility for rural telephone company status, so long as there is no common control between the rural telephone company and the other carrier. Blooston reasons that the common control definition is used in the auction rules for small businesses' affiliates, has been used by the Commission when defining connecting carriers, and is generally used by the financial community and the Securities and Exchange Commission. Finally, Blooston requests that the Commission amend its designated entity provisions to allow rural telephone companies to combine into consortia and partner with investors without losing designated entity status so long as the majority equity control resides with members who are rural telephone companies. NTCA similarly requests that the term "affiliates" be clarified to indicate what organizational structures are permitted.

87. *Discussion.* In response to the requests of NTCA and Blooston that we clarify the meaning of the term affiliate to indicate the types of organizational structures that will be included, we amend the *Second Report and Order* to establish as our standard affiliation rules the same affiliation

[127] SDN argues that the Commission should allow rural telephone companies to form consortia among themselves, since combining telephone companies does not alter their rural nature. SDN also argues that consortia with investors should be permitted so long as the rural telephone company retains at least 50.1 percent equity and control. SDN Petition at ¶ ¶ 20-23.

[128] *See Second Report and Order* at ¶ 286.

rules adopted by the Commission in the *Fifth Report and Order*.[129] Blooston specifically requests that we clarify the meaning of "affiliate" so that passive investments by a rural telephone company in other rural telephone companies do not preclude designated entity status if there is no common control. As described more fully below, under our affiliation rules a passive interest in another telephone company, which does not constitute control of that company would not be considered an affiliation for purposes of access line aggregation.

88. In the *Second Report and Order*, we referenced the SBA's affiliation rules for purposes of defining generally whether an entity qualifies as a small business and gave examples of how the affiliation rules would be applied. In the *Fifth Report and Order* we expanded on the SBA's affiliation rules in establishing detailed affiliation standards for broadband PCS to be used in the context of determining designated entity eligibility where our criteria are based on the size of the entity seeking special treatment and require applicants to include "affiliates" when calculating their eligibility. These affiliation requirements are intended to prevent entities that do not meet these size standards from receiving benefits targeted to smaller entities.[130] We believe that these rules are appropriate for determining affiliations generally, and therefore we will incorporate these standards into our generic auction rules for purposes of determining all size-based eligibility requirements. We summarize these standards below.

89. Where we adopt sized-based eligibility rules and provide that such eligibility determinations shall include the applicant and all its "affiliates," the following rules shall govern determinations regarding affiliation. Apart from determining affiliation between the applicant itself and outside entities, the need to determine affiliation arises where an investor has an attributable interest in a designated entity.[131] In this context it is necessary for the Commission to examine whether such investor has a relationship with other persons or outside entities that rise to the level of an affiliation with the applicant, and if so, whether the affiliate's assets, revenues, net worth, number of access lines, or other applicable financial thresholds, when aggregated with the applicant's, exceed the Commission's size eligibility thresholds.

90. *General Principles of Affiliation.* An affiliation under the SBA rules would arise, first, from "control" of an entity or the "power to control it." Thus, under the SBA rules, entities are affiliates of each other when either directly or indirectly (i) one concern controls or has the power to control the other, or (ii) a third party or parties controls or has the power to control both.[132] In determining control, the SBA's rules provide generally that every business concern is considered to have one or more parties who directly or indirectly control or have the power to control it. The rules, in addition, provide specific examples of where control resides under various scenarios, such as through stock ownership or occupancy of director, officer or management positions. The rules also articulate general principles of control, and note, for example, that control may be affirmative or negative and that it is immaterial whether control is exercised so long as the power to control exists.[133] Second, an affiliation, under SBA rules, may also arise out of an "identity of interest" between or among parties.[134] We adopted these same general provisions as our affiliation rules for broadband PCS and will also incorporate them into our general affiliation rules.

91. In adopting these affiliation rules, we emphasize that these rules will not be applied in a manner that defeats the objectives of our service specific attribution rules. For example, in the context of broadband PCS, our attribution rules expressly permit applicants to disregard the gross revenues, total assets and net worth of certain passive investors, provided that an eligible control group has *de facto* and *de jure* control of the applicant.[135] Our attribution rules are designed to preserve control of the applicant by eligible entities, yet allow investment in the applicant by entities that do not meet the size restrictions in our rules. Therefore, so long as the requirements of our attribution rules are met, the affiliation rules will not be used to defeat the underlying policy objectives of allowing such passive investors. More specifically, if a control group has *de facto* and *de jure* control of the applicant, we shall not construe the affiliation rules in a manner that causes the interests of passive investors to be attributed to the applicant.

92. Applying these SBA affiliation rules, an affiliation would arise, for example, where an entity with an attributable interest in an applicant is under the control of another entity. An affiliation would also arise where an entity with an attributable interest in an applicant controls, or has the power to control, another entity. For example, if an attributable investor in an applicant is also a shareholder in a large Corporation X, when should Corporation X be deemed an affiliate of the applicant as a result of the shareholder's ownership interest in both entities? Under the SBA rules and the rules we adopt here, Corporation X would be deemed an affiliate of the applicant if the shareholder controlled or had the power to control. Corporation X, in which case, Corporation X's gross revenues must be included in determining the applicant's gross revenues.[136]

93. For purposes of determining control, ownership interests will be calculated on a fully-diluted basis. Thus, for example, stock options, convertible debentures, and agreements to merge (including agreements in principle) will generally be considered to have a present effect on the power to control or own an interest in either an outside entity or the PCS applicant or licensee. We will treat such options, debentures, and agreements generally as though the rights held thereunder had been exercised.[137] However,

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[129] See *Fifth Report and Order* at ¶ ¶ 201-217.

[130] *See, e.g., Second Report and Order* at ¶ 272.

[131] In the context of broadband PCS, we stated that, generally, investors owning more than 25 percent of the applicant's passive equity would be considered to have "attributable" interests. *See Fifth Report and Order* at ¶ 158. With regard to IVDS, we used the SBA standard to determine attributable interests, *i.e.*, control.

[132] 13 CFR § 121.401(a)(2)(i), (ii).

[133] *Id.* § 121.401(c)(1).

[134] *Id.* § 121.401(a)(2)(iii), (d).

[135] *See Fifth Report and Order* at ¶ 205.

[136] *See Fifth Report and Order* at ¶ 206.

[137] *See* 13 C.F.R § 121.401(f). SBA's rules provide the following examples to guide the application of this provision:

Example 1. If company "A" holds an option to purchase a controlling interest in company "B," the situation is treated as though company "A" had exercised its rights and had become

an affiliate cannot use such options and debentures to appear to terminate its control over or relationship with another concern before it actually does so.[138]

94. *Voting and Other Trusts.* In a similar vein, we also borrow from the SBA's rules and our own rules in other services to find affiliation under certain voting trusts in order to prevent a circumvention of eligibility rules. The SBA's rules provide that a voting trust, or similar agreement, cannot be used to separate voting power from beneficial ownership of voting stock for the purpose of shifting control of or the power to control an outside concern, if the primary purpose of the trust is to meet size eligibility rules.[139] Similarly, under the Commission's broadcast multiple ownership rules, stock interests held in trust may be attributed to any person who holds or shares the power to vote such stock, has the sole power to sell such stock, has the right to revoke the trust at will or to replace the trustee at will.[140] Also, under the broadcast rules, if a trustee has a familial, personal or extra-trust business relationship to the grantor or the beneficiary of a trust, the stock interests held in trust will be considered assets of the grantor or beneficiary, as appropriate.[141] Because we believe the broadcast rules provide more definitive guidance in this particular area, we shall use them as a model for the general affiliation rules adopted here. Thus, for example, if an investor with an attributable interest in an applicant holds a beneficial interest in stock of another firm that amounts to a controlling interest in that other firm, depending on the identity of the trustee, the other firm may be considered an affiliate and its assets and gross revenues may be attributed to the applicant.

95. *Officers, Directors and Key Employees.* Under the SBA's affiliation rules, which we adopt as our generic approach, affiliations also generally arise where persons serve as the officers, directors or key employees of another concern and they represent a majority or controlling element of that other concern's board of directors and/or management of the outside entity.[142] Thus, if a person with an attributable interest in an applicant, through his or her other key employment positions or positions on the board of another firm, controls that other firm, then the other firm will be considered an affiliate of the applicant. Such affiliations may or may not result in the applicant's exceeding our size limitations. As this rule reflects, for purposes of attributing the financial position of an outside entity in this context, officers and directors of an outside concern are not foreclosed entirely from holding attributable or non-attributable interests in an applicant. Whether or not such persons control the outside entity, we also do not want to prohibit these persons, who may be experienced in the telecommunications, finance, or communications and equipment industries, from assisting start-up companies by serving as officers or directors of the applicant. Thus, if such persons serving as officers or directors of the applicant do not control the applicant or otherwise have an attributable interest in the applicant, their outside affiliations (even if controlling) will not be considered at all for purposes of determining the applicant's eligibility under our rules.[143]

96. *Affiliation Through Identity of Interest: Family and Spousal Relationships.* Consistent with the SBA's rules, an affiliation may arise not only through control, but out of an "identity of interest" between or among parties.[144] For example, affiliation can arise between or among members of the same family or persons with common investments in more than one concern. In determining who controls or has the power to control an entity, persons with an identity of interest may be treated as though they were one person.[145] For example, if two shareholders in Corporation X are both attributable shareholders in an applicant, to the extent that together they have the power to control Corporation X, Corporation X may be deemed an affiliate of the applicant.

97. Similarly, as under the SBA rules, we will consider spousal and other family relationships in determining whether an affiliation exists. Under the SBA rules for determining small business status, for example, members of the same family may be treated as though they were one person because they have an "identity of interest."[146] Likewise, in order to determine whether individuals are economically disadvantaged, the SBA rules governing eligibility for participation in the government's "section 8(a)" program for socially and economically disadvantaged small businesses have special provisions for attributing spousal interests. The latter rules provide generally that half of the jointly-owned interests of an applicant and his or her spouse must be attributed to the applicant for purposes of determining the applicant's net worth.[147]

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owner of a controlling interest in company "B." The [annual revenues] of both concerns must be taken into account in determining size. Example 2. If company "A" has entered into an agreement to merge with company "B" in the future, the situation is treated as though the merger has taken place. [A and B are affiliates of each other].

[138] *Id.* SBA's rules provide this example:

If large company "A" holds 70 percent (70 of 100 outstanding shares) of the voting stock of company "B" and gives a third party an option to purchase 66 of the 70 shares owned by A, company "B" will be deemed to be an affiliate of company "A" until the third party actually exercises its option to purchase such shares. In order to prevent large company "A" from circumventing the intent of the regulation which [gives] present effect to stock options, the option is not considered to have present effect in this case.

[139] 13 CFR § 121.401(g).

[140] *See* 47 CFR § 73.3555 note 2(e).

[141] *Id.*

[142] *See* 13 CFR § 121.401(h). A key employee is an employee who, because of his/her position in the concern, has a critical influence in or substantive control over the operations or management of the concern.13 CFR § 121.405.

[143] SBA's size standard affiliation rules also provide that affiliations can arise in a variety of other scenarios, such as where one concern is dependent upon another for contracts and business, where firms share joint facilities, or have joint venture or franchise license agreements. To the extent we believe these rules may have general applicability we shall codify them in our affiliate rules. We caution parties that issues relating to *de facto* control of the applicant (or parties with attributable interests in the applicant) could also arise under arrangements not expressly codified in the rules.

[144] *See* 13 CFR § 121.401(a)(2)(iii).

[145] *Id.* at § 121.401(d).

[146] 13 CFR § 121.401(d).

[147] *See* 13 CFR § 124.106(a)(2)(i)(A)(1).

98. In the context of auction size-based eligibility standards at issue here, we begin by clarifying that our reason for considering spousal and kinship relationships is not to determine whether the spouse or other kin of a women-owned applicant actually is controlling the applicant, thereby violating our eligibility rules for woman-owned businesses. Our rules do not embody any presumptions concerning spousal control in that context. Rather, our objective here is to ensure both that entities are actually in need of the assistance provided by our rules and that entities otherwise ineligible under applicable size criteria do not circumvent the rules by funding family members that purport to be eligible applicants.

99. In formulating these rules, we need to consider also that, as a practical matter, it will not be possible for us prior to the auctions to resolve all questions that pertain to the individual circumstances of particular applicants. Furthermore, if we determine subsequent to an auction that a winning bidder in fact was ineligible to bid or to benefit from special provisions, such as bidding credits, because of spousal or kinship relationships, not only will authorization of service be delayed but, as discussed above, disqualified applicants may be subject to substantial penalties. In these circumstances, we think that the public interest requires that we endeavor, insofar as possible, to establish bright-line tests for determining when the financial interests of spouses and other kin should be attributed to the applicant.

100. We have decided that, for purposes of determining whether the financial limitations in our eligibility rules have been met, we will in every instance attribute the financial interests of an applicant's spouse to the applicant. This will resolve any concern that an applicant might transfer his or her assets to a spouse in order to satisfy the financial restrictions that apply to eligible entities. For example, an applicant could not transfer stock or other assets to his or her spouse and thereby dispose of interests that, if held by the applicant, would render the applicant ineligible. Just as importantly, this approach will resolve any concern that an applicant might participate in bidding by using the personal assets of an ineligible spouse, which would defeat entirely the objective of providing special financial measures for designated entities.

101. In adopting this rule, we fully recognize that instances could arise in which, if all factors were considered, attributing a spouse's financial interests to the applicant could lead to harsh results. As a general matter, however, we think it provides a workable bright-line standard that resolves fully our policy concerns and avoids undesirable ambiguity concerning the nature of our requirements. As in the SBA rules, however, one exception is clearly warranted; this affiliation standard would not apply if the applicant and his or her spouse are subject to a legal separation recognized by a court of competent jurisdiction. In calculating their personal net worth, for example, investors in the applicant who are legally separated must, of course, still include their share of interests in community property held with a spouse.

102. As indicated above, circumstances could also arise in which other kinship relationships are used as a means to evade our eligibility requirements. Because we believe kinship relationships in many cases do not present the same potential for abuse that exists with spousal relationships, particularly in terms of the "identity of interests" that are likely to exist between the persons involved, we shall adopt a more relaxed standard for determining when kinship interests must be attributed to applicants. In this area, we shall follow the same standard that is applied by the SBA when interpreting its "identity of interest" rule described above. Specifically, an identity of interests between family members and applicants will be presumed to exist, but the presumption can be rebutted by showing that the family members are estranged, or that their family ties are remote, or that the family members are not closely related in business matters.[148] For purposes of determining who is a family member under this rule, we shall use a definition that is identical to the definition of "immediate family member" in the SBA's rules, 13 CFR § 124.100.

103. In appropriate cases, an applicant should be able to rebut the presumption regarding kinship affiliations with relative ease, simply by demonstrating that the applicant has no close relationship in business matters with the relevant family members. Of course, should such business relationships arise with a winning applicant after the auction, we might need to consider whether the applicant intended to circumvent the requirements of our eligibility rules.

104. The affiliation requirement is intended to prevent entities that, for all practical purposes, do not meet the size standard required for eligibility from receiving benefits targeted to smaller entities.[149] We believe that the affiliation rules described above will accomplish this objective.

E. Rural Telephone Company Bidding Credits.

105. *Petitions.* NCTA, USIN and SDN argue that the FCC should retain the rural telephone company bidding credit provision adopted in the *Second Report and Order* but delete the accelerated build-out requirement as a condition for receipt of bidding credits. USIN asserts that bidding credits will not help attract capital when tied to such an expanded build-out requirement. According to USIN, making bidding credits contingent on an accelerated build-out effectively nullifies the provision because the commitment of additional capital for network build-out will reduce the amount available to finance the license price by enough to offset any benefit conferred by the availability of the credit.[150] SDN agrees that additional build-out should not be required as a prerequisite for rural telephone company bidding credits, but states that a rural telephone company should receive additional bidding credits if it substantially covers its certified rural service area during its license term.[151] NTCA argues that the accelerated build-out requirement for bidding credits should be eliminated since this requirement is unrelated to the statutory purpose of promoting investment in and rapid deployment of new technologies and services in rural areas.[152]

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[148] *See generally Texas-Capital Contractors, Inc. v. Abdnor*, 933 F.2d 261 (5th Cir. 1990).

[149] *See, e.g., Second Report and Order* at ¶ 272.

[150] USIN Petition at 12.

[151] SDN Petition at 14.

[152] *See* 47 U.S.C. § 309(j)(3)(A).

106. SDN also contends that the risk of forfeiting the bidding credit (plus interest) for failure to meet the expanded build-out commitment will have a chilling effect because of the difficulty of anticipating potential problems that may be encountered in attempting to extend service rapidly to remote areas. Further, SDN maintains that an accelerated build-out requirement could engender a perverse incentive for a rural telephone company that would otherwise concentrate primarily on providing PCS service in the rural portions of a BTA or MTA (which, according to SDN might be a commercially-attractive strategy because of steeper competition in urban areas), forcing it to concentrate instead on extending its network in densely-populated areas.[153]

107. Finally, SDN and USIN contend that it is inequitable to provide rural telephone companies with a less favorable bidding credit provision than other designated entities. In this regard, USIN argues that the *Second Report and Order* fails to explain why rural telephone company bidding credits should contain more restrictive terms than other designated entity bidding credits. On the contrary, SDN contends that rural telephone companies should receive a greater bidding credit than other entities, because they face higher service and construction costs. Accordingly, SDN maintains that if accelerated build-out is to be included in the rural telephone company provision, an incentive should be provided in the form of bonus credit over and above the standard bidding credit available to other designated entities.

108. *Discussion.* In the *Second Report and Order* we adopted a system of bidding credits for rural telephone companies designed to further promote the investment in and rapid deployment of new technologies and services in rural areas.[154] We generally concluded that any special measures adopted for rural telephone companies, including bidding credits, should be limited to bidding for licenses in their rural service areas. We found that this limitation satisfied Congress's objectives without unduly favoring rural telephone companies in markets where there was no compelling reason to do so. Specifically, we concluded that Congress was primarily concerned with assuring rural consumers the benefits of new technologies and providing opportunities for participation by rural telephone companies in the provision of wireless services that supplement or replace their landline facilities.[155] Accordingly, we provided that rural telephone companies would be eligible for bidding credits for specified licenses only in their service areas.

109. However, unlike bidding credits available to women and minority-owned firms, we linked the amount of the bidding credit for rural telephone companies to their commitment to achieve certain expanded infrastructure build-out requirements in their rural service areas. We provided that the amount of the bidding credit would be proportionately linked to the amount by which the rural telephone company agreed to expand its build-out commitment. In this regard, we indicated that failure to meet the expanded build-out commitment would result in liability for a penalty in the amount of the bidding credit, plus interest at the rate applicable to installment payments. We further provided that grant of the licenses to rural telephone companies utilizing bidding credits would be conditioned upon payment of this penalty, if and when it becomes applicable. We concluded that this added construction requirement would fulfill the congressional objective of developing and rapidly deploying new services to those residing in rural areas.

110. On reconsideration of this issue, we no longer believe the provision in the *Second Report and Order*, which links the availability of bidding credits for rural telephone companies to their agreement to satisfy an expanded construction requirement, is necessary or appropriate to promote the statutory objectives. We agree with petitioners' assertions that the expanded build-out requirement may have adverse consequences contrary to the purpose of bidding credit provision. We are also concerned that the expanded construction requirement may be unduly burdensome both to rural telephone company licensees and the Commission. In this regard, we are concerned that the accelerated build-out requirement may not be economically feasible in some rural areas and thus may result in frequent forfeitures of the bidding credit amount by rural telephone companies. As discussed more fully below, we now believe that Congress' objectives of promoting investment in and rapid deployment of new technologies and services to rural areas will best be achieved through the use of other provisions such as installment payments, bidding credits (without an expanded build out requirement), and service area partitioning. Thus, we amend our rules to retain flexibility to adopt any of these or other provisions for rural telephone companies on a service-specific basis after considering the characteristics and capital requirements of the particular service.

F. Rural Telephone Company Eligibility for Installment Payments

111. *Petitions.* SDN, USIN, and NCTA all request that installment payments be extended to rural telephone companies regardless of their status as small businesses. AIDE and Cook Inlet argue that all designated entities should be permitted to pay for their licenses in installment payments irrespective of their size. These parties all object to the decision to limit eligibility for installment payments to small businesses as defined in §1.2110(b)(1), *(i.e.,* companies with net worth including that of affiliates of $6 million or less and no more than $2 million of annual after-federal-tax profit for the last two years). USIN argues that there is no statutory support in the provisions cited by the Commission as authority for adopting different provisions for one designated entity group as opposed to another.

112. Citing the legislative history to the Budget Act and H.R. Report No. 103-111 in particular, USIN also maintains that the statutory purpose of requiring special provisions for designated entities was to promote entry by firms with difficulty in obtaining access to capital. Petitioners maintain that the $6million net worth$2 million net revenue standard for installment payment eligibility is too strict and will prevent rural telephone companies from qualifying for the installment payment option although they face significant difficulty in obtaining access to capital. USIN asserts that as a practical matter rural telephone

153 SDN Petition at 14-15.
154 *See* 47 U.S.C. § 309(j)(3)(A).
155 *Second Report and Order* at ¶ 243.

companies may have high levels of non-amortized assets and yet have less capital available for investment than many businesses that meet the small business definition. SDN maintains that rural telephone companies should be eligible for installment payments regardless of whether they qualify as small businesses because they will generally incur higher build out costs with lower revenue streams than other designated entities. According to USIN, a rural telephone company bidding for a license in a capital-intensive service should be eligible for installment payments if its annual revenue are under $100 million USIN asserts that without installment payments such telephone companies will be unable to bid for broad-coverage licenses as traditional rural telephone company lenders have indicated unwillingness to finance auction bids.

113. AIDE objects to the determination in the *Second Report and Order* that limits the installment payment option to small businesses bidding on licenses for "those smaller spectrum blocks that are most likely to match the business objectives of *bona fide* small businesses."[156] According to AIDE, such the installment payment option should be available to all designated entities bidding on all licenses. AIDE maintains that Congress did not intend to give the FCC discretion to offer special provisions to some designated entities in some auctions but not in others. AIDE argues, moreover, that these limitations on the availability of installment payments are not justified by the Commission's desire to prevent abuse of its designated entity provisions since there are other safeguards designed specifically for that purpose, such as the rules for disclosure of real parties in interest, the definitional requirements including the assets of affiliates and the financial qualification rules.

114. *Discussion.* For the reasons set forth below, we deny petitioners' requests to expand the installment payment option to other designated entities irrespective of their economic status. However, we will retain the flexibility to expand or modify the installment payment option on a service-specific basis for other appropriately-sized entities where the spectrum costs and capital infrastructure requirements necessitate their application to other entities. For example, in the *Fifth Report and Order* we recognized that the substantial expected capital required to acquire and construct broadband PCS licenses warranted expansion of the installment payment option to most entities acquiring licenses in the entrepreneurs' blocks.[157] Under the broadband PCS rules, installment payments are available to smaller entities that do not technically qualify as small businesses and an enhanced installment payment option is available to eligible small businesses and businesses owned by women and/or minorities.

115. In the *Second Report and Order,* we concluded that for some auctions, small businesses would be eligible for installment payments. We noted that by allowing payment in installments, the government would be extending credit to an eligible winning bidder, thus reducing the amount of private financing needed in advance of the auction by a prospective licensee. We noted that this will assist small entities who are likely to have difficulty obtaining adequate private financing. As a result, we concluded that installment payments would be an effective way to promote efficiently the participation of small businesses in the provision of spectrum-based telecommunications service and an effective tool for efficiently distributing licenses and services among geographic areas.[158] Thus, we limited application of installment payments to small entities, including such entities that are owned by minorities and/or women. We found that this approach best served the intent of Congress in enacting section 309(j)(4)(A), to avoid a competitive bidding program that has the effect of favoring incumbents, with established revenue streams, over new companies or start-ups.[159]

116. Consistent with Congress's concern that auctions not operate to exclude small businesses, the provisions relating to installment payments for minorities and/or women also were intended to assist only minorities and women who are small businesses. The House Report states that these related provisions were drafted to "ensure that *all small businesses* will be covered by the Commission's regulations, *including those owned by members of minority groups and women.*"[160] (emphasis added). It also states that the provisions in section 309(j)(4)(A) relating to installment payments were intended to promote economic opportunity by ensuring that competitive bidding does not inadvertently favor incumbents with "deep pockets" "over new companies or start-ups."[161] Because the Congressional objective here was to assist "new companies or start-ups," we therefore concluded that the Commission should use installment payments only for smaller sized entities. As indicated by the legislative history, large entities with established revenue streams were not intended to be beneficiaries of this particular means of financial assistance. We concluded that the statutory language, when read in conjunction with the legislative history, does not indicate that Congress's purpose was to accord special financial assistance measures under section 309(j)(4)(A) to entities other than those with small economic status.[162] In this regard, we reject petitioner's proposals to allow installment payments for rural telephone companies or other designated entities irrespective of their size. We will continue to determine on a service-specific basis the appropriate economic eligibility criteria for installment payments. And we may, as we did in the context of broadband PCS, establish different installment payment options for entities who face different economic barriers.

117. In addition, and consistent with our decision to limit installment payments to small entities, we decline to make installment payments available for all licenses in all auctions. Rather, in order to match the provisions with eligible recipients, we will continue to make installment payments available only for certain licenses that do not involve the largest spectrum blocks and service areas. In this regard, in the context of narrowband PCS, we adopted installment payments only for the regional, MTA and BTA licenses. Similarly, for broadband PCS, we limited eligibility for installment payments to the BTA licenses contained

156 *See Second Report and Order* at ¶ 237.
157 *See Fifth Report and Order* at ¶ ¶ 136-140.
158 *See Second Report and Order* at ¶ ¶ 233-240.
159 *See* H.R. Rep. No. 103-111 at 255.
160 *Id.*
161 *Id.*

162 Under authority of Section 309(j)(4))(D), we have, however, afforded other types of financial assistance measures, such as bidding credits, to other designated entities. *See e.g., Third Report and Order,* in PP Docket No. 92-253, 59 FR 2674 (May 24, 1994), at ¶ ¶ 72-81 (which provides bidding credits to businesses owned by minorities and/or women).

in the entrepreneurs' blocks. We continue to believe that where large, valuable blocks of spectrum are being auctioned we should not give ineligible entities the incentive to create small business "fronts," thereby enabling large businesses to become eligible for low-cost government financing. Nor do we desire to delay service to the public by encouraging under-capitalized firms to receive licenses for facilities which they may lack the resources adequately to finance.[163] Accordingly, we will continue to allow installment payments only for licenses in those smaller spectrum blocks and service areas that are most likely to match the business objectives of *bona fide* small entities in the context of a particular service. The particular spectrum block sizes that will be eligible for installment payments will be decided in the context of each particular service taking into account the cost of acquiring the spectrum and constructing the system.

G. Rural Telephone Company Partitioning

118. *Petitions.* SDN requests that rural telephone companies be allowed to partition their rural service areas either pursuant to an agreement with the BTA or MTA licensee, or by licensing a separate PCS service area using a system similar to the cellular unserved area application process.[164]

119. Several commenters responding to the NPRM in this proceeding suggested that the Commission allow partitioning of PCS licenses so as to permit rural telephone companies to hold licenses to provide service only in their service areas.[165] In the *Second Report and Order* we recognized that partitioning may be an effective means to achieve Congress's goal of ensuring that advanced services are provided in rural areas.[166] In the context of broadband PCS, we adopted a system of geographic partitioning, for rural telephone companies which allows rural telephone companies to acquire partitioned broadband PCS licenses in one of two ways: (1) they may form bidding consortia to participate in auctions, and then partition the licenses won among consortia participants, or (2) they may acquire partitioned broadband PCS licenses from other licensees through private negotiation and agreement either before or after the auction (provided the partitioned area is reasonably related to the size of the rural telephone company's rural service area).[167] We require that partitioned areas conform to established geopolitical boundaries and that each area include the wireline service area of the rural telephone company applicant. We believe that this system of partitioning of rural service areas will provide a significant opportunity for many of these designated entities who desire to offer PCS to their customers as a complement to their local telephone services. Therefore, we will retain the flexibility in the generic auction rules to adopt a system of partitioning on a service-specific basis where the capital requirements and construction costs are such that a system is necessary to assist rural telephone companies who cannot afford or do not desire to bid for or construct systems for an entire service area.[168]

H. Unjust Enrichment Provisions

120. *Petitions.* AIDE requests that when the Commission recaptures the benefits accruing to a designated entity pursuant to the unjust enrichment provisions, the unjust enrichment penalty should credit the licensee's pre-sale investments in the license and should be based on the portion of the licensee's taxable gain on the sale allocated to the license, with appropriate adjustments. BET similarly requests that the Commission revise the unjust enrichment provisions to credit the designated entity for its pre-transfer expenditures on the license including construction costs.

121. *Discussion.* We deny the requests of AIDE and BET. In the *Second Report and Order* the Commission crafted unjust enrichment provisions designed to prevent designated entities from profiting by the rapid sale of licenses acquired through the benefit of provisions and policies meant to encourage their participation in the provision of spectrum-based services. These rules were intended to deter designated entities from prematurely transferring licenses obtained through the benefit of provisions designed to create opportunities for such designated entities in the provision of spectrum-based services. We sought through our unjust enrichment provisions to discourage designated entities who do not intend to provide service to the public from abusing our provisions by obtaining a license at a lower cost than other licensees and then selling the license after a short time to a non-designated entity at a profit. In addition, the unjust enrichment rules were intended to recapture for the government a portion of the value of the bidding credit or other special provision if such a designated entity prematurely transfers its licenses to an ineligible entity, thereby frustrating the government's efforts to encourage the inclusion of designated entities in the provision of new spectrum-based services.

122. We recognize that over time, a designated licensee may have made substantial investments in a license prior to transfer. In order to reward efficiency and encourage such investments in infrastructure development, we provided that we will generally reduce the amount of the recapture penalty as time passes or construction benchmarks are met.[169] We further provided that our recapture provisions would not apply to the transfer or assignment of a license that has been held for more than five years.[170] In addition, where a recapture penalty is assessed, we stated that the penalty will not prevent the transferring designated entity from recovering the depreciated value of its capital investment. Moreover, we indicated that in appropriate circumstances, we might waive recapture "if the licensee has incurred substantial start-up costs or made significant capital investments with the intention of starting service, but due to circumstances beyond its control, was unable to provide service."[171]

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163 *See* 47 U.S.C. § 309(j)(3)(A).

164 *See* SDN Petition at 7.

165 *See, e.g.,* comments of GVNW at 2-4, and NTCA at 13.

166 *See Second Report and Order* at ¶ 243 n.186.

167 *See Fifth Report and Order* at ¶15 2.

168 In a Further Notice of Proposed Rulemaking in this docket, the Commission will also explore the merits of allowing businesses owned by minorities and/or women to acquire partitioned PCS licenses, as well as partitioned licenses in other services.

169 *See Second Report and Order* at ¶ 262.

170 *Id.*

171 *Id.* at n.205.

123. We believe that these measures adequately account for a designated entity's pre-transfer investments in a license, including construction expenses. Therefore, we decline to adopt AIDE's proposal that we credit the licensee's pre-sale investments in the license and base the recapture amount on the portion of the licensee's taxable gain on the sale allocated to the license, because such provisions would require the government to undertake lengthy and complex accounting and allocation proceedings to determine the amount of the penalty. Similarly, we deny BET's request that we credit designated entities for their pre-transfer expenditures on a license because we believe that our recapture provisions adequately account for these expenditures by reducing the amount of the penalty over time. Moreover, the unjust enrichment provisions were designed to act as a penalty to deter premature license transfers by designated entities. Therefore we decline to modify the recapture provisions adopted in the *Second Report and Order*. We note, however, that because license terms and construction requirements vary by service, and because we may adopt different designated entity provisions for different services, we will set forth the specific recapture provisions in the service-specific competitive bidding rules of each auctionable service. Moreover, we modify our general recapture provisions to provide flexibility on a service-specific basis to extend the duration of the recapture provisions beyond five years.

I. Upfront Payment Amount

124. *Petitions.* AIDE requests that the Commission reduce the amount of the upfront payment for designated entities. AIDE asserts that a reduced upfront payment would help ensure that capital constrained designated entities have the opportunity to participate in the competitive bidding process. According to AIDE, a reduced upfront payment is necessary to create opportunities for designated entities to participate in competitive bidding and will allow such entities to preserve their limited resources for post-auction infrastructure development.

125. *Discussion.* The Commission adopted an upfront payment requirement in order to ensure that only serious, qualified bidders participate in our auctions. We reasoned that an upfront payment requirement would ensure the validity of the information generated during auctions and increase the likelihood that licenses will be awarded to the qualified bidders who value them the most, thus promoting the rapid deployment of new technology. Upfront payments will also provide the Commission with a source of available funds in the event a bid withdrawal penalty must be assessed. By requiring a substantial upfront payment amount, the Commission seeks to deter speculative and frivolous bidding by all bidders, including designated entities. Moreover, the standard upfront payment formula ($.02 per MHz per pop for the maximum MHz-pops a bidder intends to bid on in any single round of bidding), is based on the amount of spectrum and population coverage on which a bidder seeks to bid and therefore is directly linked to the expected value of the license and anticipated construction costs a licensee will incur.

126. Nevertheless, in the *Second Report and Order* we retained the flexibility to cap, reduce or modify the upfront payment amount for designated entities.[172] We indicated that such decisions would be made in the service-specific competitive bidding rules for individual services. In the *Fifth Report and Order,* recognizing that the standard upfront payment formula may create a barrier for smaller entities wishing to participate in auctions, we reduced by 25 percent the upfront payment amount required for designated entities bidding in the entrepreneur's blocks.[173] Given the varied spectrum costs of different services, we will continue to consider such reduced upfront payments for designated entities on a service-specific basis. Generally, we will only reduce the upfront payment amounts for designated entities in capital intensive services, such as broadband PCS, where the spectrum bandwidth will result in upfront payment amounts that may be prohibitive for some smaller entities.

J. Installment Payments

127. In the *Second Report and Order,* we stated that, for some auctions, winning bidders that are small businesses would be eligible to use installment payments in paying for licenses.[174] We provided that for these winning bidders, a down payment of 10 percent would be due within five business days of the close of the auction, and that an additional 10 percent would be due within five days of grant of the license.[175] We stated that we would impose interest on installment payments at a rate equal to the rate for U.S. Treasury obligations of maturity equal to the license term. We stated that the schedule of installment payments would begin with interest-only payments for the first two years, and that thereafter principal and interest would be amortized over the remaining term of the license.[176]

128. Upon reconsideration, we have decided that we may need to tailor installment payment provisions more precisely to needs of various groups of designated entities and the characteristics of particular services. In the *Fifth Report and Order* we provided installment payments for minorities and women in some blocks, and provided different installment provisions for small businesses of different sizes.[177] We will continue to establish different installment payment provisions on a service-specific basis. We may offer installment payments to minorities and women, in some circumstances, and may offer installment payments having differing terms to different classes of designated entities. We may vary the interest rate and the payment schedule for installment payments, including the amount and timing of the down payment and the schedule for amortization of principal and interest. Installment payment provisions for each service will be specified in Orders establishing auction rules for that service. We believe that this additional flexibility will allow us to take account of differences in capital requirements across services and license blocks, and to provide access to capital in ways that will give various groups of designated entities a realistic chance to participate in offering service.

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172 *See Second Report and Order* at ¶ 178 n.37.
173 *See Fifth Report and Order* at ¶ 156.
174 *Id.* at ¶ 233.
175 *Id.* at ¶ 238.
176 *Id.* at ¶ 239.
177 *Fifth Report and Order* at ¶ ¶ 137-139.

K. Eligibility Issues

129. *Petitions.* Black Entertainment Television Holdings, Inc. (BET) requests that the FCC reconsider the public company restriction on the availability of provisions for minority and women-owned companies in broadband PCS. BET argues that given the costs of acquiring spectrum and the construction expense, such a limitation would defeat realistic opportunities for a wide range of minority-owned firms. BET also requests that we clarify that provisions for minority and women-owned firms are separate and distinct from provisions for small businesses. Finally, BET argues that rights, privileges, options or other forms of ownership that do not affect the ability of a designated entity to control a company, or diminish a designated entity financial stake in a venture, should not be considered in the definitional analysis for purposes of determining eligibility.

130. *Discussion.* In the *Second Report and Order,* we stated that publicly traded minority and women-owned companies would not be eligible for provisions applicable to these designated entities. In the *Fifth Report and Order,* however, we deviated from this restriction to allow publicly traded minority and women-owned companies to qualify to bid in the entrepreneurs' block, and under certain circumstances to qualify for bidding credits.[178] We will continue to consider exceptions to our restriction on publicly traded company eligibility for minority and women-owned businesses on a service-specific basis, in each case considering the capital requirements and the expected build-out cost of the service. We agree with BET that in services with high entry costs, precluding publicly traded companies from receiving measures intended for minority and women-owned businesses may undermine our objective of ensuring the opportunity for these designated entities to participate in the provision of spectrum-based services.

131. As requested by BET, we clarify that the provisions for businesses owned by women and minorities are separate and distinct from the provisions for small businesses. Thus, women and minority-owned businesses may qualify for measures adopted for these entities irrespective of their size, and small businesses may qualify for small business provisions regardless of their ownership by minorities and women. And small businesses that are owned by members of minorities and/or women may qualify for provisions applicable to both groups.

132. Finally, in the general auction rules, we indicated that in determining designated entity eligibility we would consider all rights, warrants and options on a fully diluted basis, *i.e.,* they will be treated as if already exercised.[179] We intend to maintain the existing rule of calculating these ownership interests on a fully diluted basis, since we expect that such ownership interests will almost always have the potential either to impact the ability of a designated entity to control a company or to diminish a designated entity's financial stake in the venture. However, in the rare circumstance where such ownership interests have no effect on a designated entity's ability to control a firm or to diminish the designated entity's financial stake, we will consider requests for waivers.[180] We note, however, that we expect such instances to be rare, and petitioners will be required to make an affirmative showing sufficient to overcome the presumption that such ownership interests should be calculated as if exercised for purposes of determining eligibility issues.

133. *Petitions.* AIDE and Cook Inlet propose stricter eligibility and anti-sham measures to avoid designated entity shams. Specifically, Cook Inlet proposes requiring that a designated entity maintain clear structural control of an entity in order to be eligible for designated entity provisions. In this regard, Cook Inlet argues that in limited partnerships, the general partner should be required to be a designated entity and restrictions should be imposed on the ability of other general partners to exercise management control. Cook Inlet also proposes that the Commission require designated entities to document their eligibility by attaching documentation to their long form application.

134. We agree with AIDE that in some instances stricter eligibility requirements are appropriate to ensure that only legitimate designated entities are the beneficiaries of the special provisions established under our rules. In particular, we clarify that, when an applicant or a licensee is a partnership, because each general partner generally has the ability to act on behalf of the partnership, all general partners in the license applicant must be designated entities in order to qualify for designated entity status. We believe that this clarification is consistent with the Commission's long-standing practice of attributing control in the context of partnerships to the general partners. This clarification will ensure that designated entities in partnerships retain *de facto* as well as *de jure* control.

135. In addition, we agree with AIDE that documentation of designated entity status should be submitted along with the applicants' long-form applications in order to enable the Commission to verify designated entity eligibility. Accordingly, we will require designated entities to substantiate their eligibility by describing on their long-form application how they satisfy the requirements for eligibility. We will also require designated entity applicants to list on their long-form application all agreements that effect designated entity status, such as all partnership agreements, shareholder agreements, management agreements and other agreements, including oral agreements, which establish that the designated entity will have both *de facto* and *de jure* control of the entity. In addition, we will require that such information be maintained at the licensee's facilities, or by its designated agent, for the term of the license, and that the information be made available to Commission staff upon request in order to enable the Commission to audit designated entity eligibility on an ongoing basis.

136. In addition, if an applicant for designated entity status proves unqualified, and the Commission determines that the application for designated entity status involved willful misrepresentation or other serious misconduct, the Commission will impose severe penalties. These may include monetary forfeitures, revocation of licenses, and prohibition of participaton in future auctions.

137. With respect to AIDE's proposal that clear structural control should be required to establish designated entity eligibility, we believe that as a general rule, our strict requirement that women and minority principals control the applicant and maintain a 50.1 percent voting interest (in a corporate applicant) and a 50.1 percent eq-

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178 *See Fifth Report and Order* at ¶ ¶ 163-164.
179 47 CFR Sec. 1.2110 (b)(2).
180 *See* 47 CFR Sec. 1.2110.

uity stake in the entity is sufficient to prevent "fronts" and to ensure that our provisions are only made available to legitimate qualified designated entities. However, we reserve the flexibility on a service-specific basis, taking into account the nature of the specific provisions applicable in that service, to adopt additional or different requirements for designated entity eligibility.[181]

138. While we conclude that our requirement that control and substantial equity rest with minorities and/or women will generally be adequate to ensure that parties do not attempt to evade the statutory requirement to provide economic opportunities and ensure participation by businesses owned by these groups, we also reaffirm our commitment to investigate all allegations of fronts, shams or other methods used to try to evade our eligibility rules. In this regard, we remind parties that we will conduct random pre and post-auction audits to ensure that applicants receiving designated entity benefits are *bona fide* designated entities.

L. Small Businesses

139. *Petitions.* NTCA and USIN request that we amend the small business definition so that it can be flexibly modified in the context of a particular service. NTCA and USIN advocate that such flexibility is appropriate because the existing $6 million net worth$2 million net income test is too low to reflect the capital-intensive nature of the broadband PCS business. NTCA asserts that most rural telephone companies are unable to meet this test even though they have few subscribers and very few employees. USIN states that the current definition discriminates against small rural telephone companies, and that the proper measure for small businesses in capital-intensive services is those with annual revenues of less than $100 million.

140. *Discussion.* We agree with NTCA. In the *Second Report and Order* we relied on the Small Business Administration's (SBA) standard definition. The SBA definition permits an applicant to qualify for financial assistance based on a net worth not in excess of $6 million with average net income after Federal income taxes for the two preceding years not in excess of $2 million.[182] The record in this proceeding reflected broad disagreement about the appropriate definition of small businesses. Many commenters, including the Chief Counsel for Advocacy of the SBA, argued that the SBA net worth/revenue definition was too restrictive and would exclude businesses of sufficient size to survive, much less succeed, in the competitive wireless communications marketplace. The SBA's Chief Counsel for Advocacy and Suite 12 Group advocated adoption of a revenue test, arguing that a net worth test could be misleading as some very large companies have low net worth. The SBA's Chief Counsel recommended that the revenue standard be raised to include firms that (together with affiliates) have less than $40 million in revenue. The SBA Chief Counsel suggested that the Commission consider a higher revenue ceiling or adopt different size standards for different telecommunications markets.[183]

141. Other parties indicated that the definition used by the Commission might impede the ability of small businesses to raise capital in anticipation of auctions. They noted that many small firms are soliciting investors to enable these firms to compete better in auctions, and argued that their designated entity status should not be jeopardized as a result. Thus, these commenters suggested, if the FCC adopts the SBA's net worth standard, the net worth valuation should relate back to the date of the PCS Final Report and Order (September 23, 1993).

142. In contrast, several commenters argue that the small business definition must be made more restrictive in order to prevent large firms from spinning off companies to compete as designated entities. In this regard, some parties recommend limiting provisions to those small businesses that were in existence for the previous two years.

143. In the *Second Report and Order,* we adopted the existing SBA net worth/net income size standard as the generic threshold for small businesses to qualify as designated entities because at that time we were unable to conclude that the other proposals suggested by commenters were superior to this established standard. However we acknowledged that for certain telecommunications industry sectors this standard may not be high enough to encompass those entities that require the benefits, but also have the financial wherewithal to construct and operate the systems. Accordingly, we indicated that this "threshold could be adjusted upward on a service-by-service basis to accommodate such situations." We also noted that we may modify the small business definition if the SBA changed its definition or the Commission determined that an alternative definition was more appropriate for capital intensive services.

144. In this regard, in the *Fifth Report and Order* we revised the definition of a small business set forth in the *Second Report and Order* to include entities with up to $40 million in gross revenues, and we provided that these small businesses would be permitted to pool their resources and form consortia to bid in the entrepreneurs' blocks or to receive other small business benefits. We also adopted rules that allow small businesses and businesses owned by women and/or minorities to raise capital by selling passive ownership interests in their companies. Thus, for example, under certain conditions, businesses owned by women and minorities have the option of taking on one large passive partner (holding up to 49.9 percent of the enterprise) or selling a greater portion of their companies' equity (up to 75 percent of the equity) to passive investors in smaller increments. Either of these structures should enhance the

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[181] For example, in the *Fifth Report and Order* we allowed minority or women-owned broadband PCS applicants to sell up to 75 percent of the company's equity to passive investors so long as the control groups retained control and 25 percent of the equity and each other investor owned less than 25 percent of the passive equity. We also established control group tests for small businesses and entities that wished to bid in certain blocks.

[182] 13 CFR 121.802.

[183] Some parties recommend using the SBA's 1500 employee standard. *See, e.g.,* comments of SBA Associate Administrator for Procurement Assistance at 2, CFW Communications at 2, and Iowa Network at 17. A number of other commenters argue, however, that adoption of this alternative SBA definition would open up a huge loophole in the designated entity eligibility criteria. Specifically, they contend that telecommunications is a capital, rather than labor, intensive industry, and that an entity with 1,500 employees is likely to be extremely well capitalized and have no need for the special treatment outlined by Congress in the Budget Act. *See, e.g.,* comments of LuxCel Group, Inc. at 4, Suite 12 Group at 10-11.

ability of these entities to obtain the necessary funding to meet long-term construction, operation and expansion goals.[184]

145. Given the diversity of services that may be subject to competitive bidding and the varied spectrum costs and build-out requirements associated with each, we conclude that it is more appropriate to define the eligibility requirements for small businesses on a service-specific basis, taking into account the capital requirements of each particular service in establishing the appropriate threshold. Therefore we will amend our generic auction rules to replace the small business definition with a provision enabling the Commission to establish a small businesses definition in the context of each particular service.

V. FINAL REGULATORY FLEXIBILITY ANALYSIS

146. Pursuant to the Regulatory Flexibility Act of 1980, 5 U.S.C. § 604, the Commission's final analysis is as follows:

A. Need for, and Purpose of, this Action

147. As a result of new statutory authority, the Commission may utilize competitive bidding mechanisms in the granting of certain initial licenses. The Commission published an Initial Regulatory Flexibility Analysis, *see generally* 5 U.S.C. § 603, within the *Notice of Proposed Rule Making* in this proceeding, and published a Final Regulatory Flexibility Analysis within the *Second Report and Order* (at ¶ ¶ 299-302). As noted in these previous final analyses, this proceeding will establish a system of competitive bidding for choosing among certain applications for initial licenses, and will carry out statutory mandates that certain designated entities, including small entities, be afforded an opportunity to participate in the competitive bidding process and in the provision of spectrum-based services.

B. Summary of the Issues Raised by the Public Comments in Response to the Initial Regulatory Flexibility Analysis

148. No comments were submitted in response to our Initial Regulatory Flexibility Analysis.

C. Significant Alternatives Considered

149. Although, as described in (B) above, no comments were received pertaining to our Initial Regulatory Flexibility Analysis, the *Second Report and Order* addressed at length the general policy considerations raised as a result of the Commission's new auction authority.

VI. PROCEDURAL MATTERS AND ORDERING CLAUSES

150. Accordingly, IT IS ORDERED, that the petitions for reconsideration ARE GRANTED to the extent described above and DENIED in all other respects, and that the petition of William E. Zimsky IS DISMISSED as moot.

151. IT IS FURTHER ORDERED, that Part 1 of the Commission's Rules IS AMENDED as set forth in Appendix B, attached. IT IS ORDERED that the rule changes made herein WILL BECOME EFFECTIVE 30 days after their publication in the Federal Register. This action is taken pursuant to Sections 4(i), 303(r) and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 303(r) and 309(j).

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

APPENDIX A

FILINGS IN RESPONSE TO THE SECOND REPORT AND ORDER

Petitions

Anchorage Telephone Utility (ATU, Anchorage)

John G. Andrikopoulos, et al. (Andrikopoulos)

The Association of Independent Designated Entities (AIDE)

Black Entertainment Television Holdings, Inc. (BET)

Dennis C. Brown and Robert H. Schwaninger, Jr. (Brown & Schwaninger)

Blooston, Mordkofsky, Jackson & Dickens (Blooston)

Cable and Wireless, Inc. (CWI)

Cook Inlet Region, Inc. (CIRI, Cook Inlet)

GTE Service Corporation and Affiliates (GTE)

Houston, Dallas, Oxnard and Huntington Cellular Settlement Groups (Cellular Settlement Groups)

MCI Telecom. Corp. (MCI)

Millin Publications, Inc. (Millin)

The National Assoc. of Business and Educational Radio (NABER)

The National Telephone Cooperative Association (NTCA)

The Rural Cellular Association (RCA)

South Dakota Network, Inc. (SDN)

Southwestern Bell Corporation (SBC)

Telephone and Data Systems, Inc. (TDS)

Thumb Cellular Limited Partnership (Thumb Cellular)

U.S. Intelco Networks, Inc. (USIN)

William E. Zimsky (Zimsky)

Oppositions and Comments

Black Entertainment Television Holdings, Inc. (BET)

Quentin L. Breen (Breen)

GTE Service Corp. and Affiliates (GTE)

[184] *See Fifth Report and Order* at ¶185.

MCI Telecom. Corp. (MCI)

Pacific Bell and Nevada Bell (Pacific Bell)

Telephone and Data Systems, Inc. (TDS)

Tri-County Telephone Company, Inc. (Tri-County)

The United States Telephone Association (USTA)

Replies

Anchorage Telephone Utility (ATU, Anchorage)

The Association of Independent Designated Entities (AIDE)

Houston, Dallas, Oxnard and Huntington Cellular Settlement Groups (Cellular Settlement Groups)

The National Telephone Cooperative Association (NTCA)

The Rural Cellular Association (RCA)

APPENDIX B

FINAL RULES

Part 1 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

1. The authority citation for Part 1 continues to read as follows:

AUTHORITY: Secs. 1, 4(i), 303, 48 Stat. 1066, 1082, as amended; 47 U.S.C. §§ 151, 154, and 303, unless otherwise noted.

2. Subpart Q of Part 1 is amended to read as follows:

Subpart Q - Competitive Bidding Proceedings

AUTHORITY: 47 U.S.C. 309(j).

GENERAL PROCEDURES

§ 1.2101 Purpose

The provisions of this subpart implement Section 309(j) of the Communications Act of 1934, as added by the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66), authorizing the Commission to employ competitive bidding procedures to choose from among two or more mutually exclusive applications for certain initial licenses.

§ 1.2102 Eligibility of Applications for Competitive Bidding

(a) Mutually exclusive initial applications in the following services or classes of services are subject to competitive bidding:

(1) Interactive Video Data Service (*see* 47 CFR Part 95, Subpart F). This subsection does not apply to applications which were filed prior to July 26, 1993;

(2) Marine Public Coast Stations (*see* 47 CFR Part 80, Subpart J);

(3) Multipoint Distribution Service and Multichannel Multipoint Distribution Service (*see* 47 CFR Part 21, Subpart K). This subsection does not apply to applications which were filed prior to July 26, 1993;

(4) Exclusive Private Carrier Paging above 900 MHz (*see* 47 CFR Part 90, Subpart P and the Private Carrier Paging Exclusivity Report and Order, 8 FCC Rcd 8318, 58 FR 62289 (Nov 26, 1993));

(5) Public Mobile Services (*see* 47 CFR Part 22), except in Hthe 800 MHz Air-Ground Radiotelephone Service, and in the Rural Radio Service. This subsection does not apply to applications in the cellular radio service, such as cellular unserved area applications, that were filed prior to July 26, 1993;

(6) Specialized Mobile Radio Service (SMR) (*see* 47 CFR Part 90, Subpart S) including aplications based on finder's preferences for frequencies allocated to the SMR service (*see* 47 CFR Section 90.173);

(7) Personal Communications Services (PCS) (*see* 47 CFR Part 24); and

NOTE: To determine the rules that apply to competitive bidding in the foregoing services, specific service rules should also be consulted.

(b) The following types of license applications are not subject to competitive bidding procedures:

(1) Applications for renewal of licenses;

(2) Applications for modification of license; provided, however, that the Commission may determine that applications for modification that are mutually exclusive with other applications should be subject to competitive bidding;

(3) Applications for subsidiary communications services. A "subsidiary communications service" is a class of service where the signal for that service is indivisible from that of the main channel signal and that main channel signal is exempt from competitive bidding under other provisions of these rules. *See, e.g.,* § 1.2102(c) (exempting broadcast services). Examples of such subsidiary communications services are those transmitted on subcarriers within the FM baseband signal (*see* 47 CFR § 73.295), and signals transmitted within the Vertical Blanking Interval of a broadcast television signal; and

(4) Applications for frequencies used as an intermediate link or links in the provision of a continuous, end-to-end service where no service is provided directly to subscribers over the frequencies. Examples of such intermediate links are (a) point-to-point microwave facilities used to connect a cellular radio telephone base station with a cellular radio telephone mobile telephone switching office and (b) point-to-point microwave facilities used as part of the service offering in the provision of telephone exchange or interexchange service.

(c) Applications in the following services or classes of services are not subject to competitive bidding:

(1) Alaska-Private Fixed Stations (*see* 47 CFR Part 80, Subpart O);

(2) Broadcast radio (AM and FM) and broadcast television (VHF, UHF, LPTV) under 47 CFR Part 73;

(3) Broadcast Auxiliary and Cable Television Relay Services (*see* 47 CFR Part 74, Subparts D, E, F, G, H and L and Part 78, Subpart B);

(4) Instructional Television Fixed Service (*see* 47 CFR Part 74, Subpart I);

(5) Maritime Support Stations (*see* 47 CFR Part 80, Subpart N);

(6) Marine Operational Fixed Stations (*see* 47 CFR Part 80, Subpart L);

(7) Marine Radiodetermination Stations (*see* 47 CFR Part 80, Subpart M);

(8) Personal Radio Services (*see* 47 CFR Part 95), except applications filed after July 26, 1993, in the Interactive Video Data Service (*see* 47 CFR Part 95, Subpart F);

(9) Public Safety, Industrial/Land Transportation, General and Business Radio categories above 800 MHz , including finder's preference requests for frequencies not allocated to the SMR service (*see* 47 CFR Section 90.173), and including, until further notice of the Commission, the Automated Vehicle Monitoring Service (*see* 47 CFR § 90.239);

(10) Private Land Mobile Radio Services between 470-512 Mhz (*see* 47 CFR Part 90, Subparts B-F), including those based on finder's preferences, *see* 47 CFR Section 90.173;

(11) Private Land Mobile Radio Services below 470 MHz (*see* 47 CFR Part 90, Subparts B-F) except in the 220 MHz band (*see* 47 CFR Part 90, Subpart T), including those based on finder's preferences (*see* 47 CFR Section 90.173); and

(12) Private Operational Fixed Services (*see* 47 CFR Part 94).

§ 1.2103 Competitive Bidding Design Options

(a) The Commission will select the competitive bidding design(s) to be used in auctioning particular licenses or classes of licenses on a service-specific basis. The choice of competitive bidding design will generally be made pursuant to the criteria set forth in the Second Report and Order in PP Docket No. 93-253, FCC 94-61, 59 FR 22980 (May 4, 1994), adopted March 8, 1994, but the Commission may design and test alternative methodologies. The Commission will choose from one or more of the following types of auction designs for services or classes of services subject to competitive bidding:

(1) Single round sealed bid auctions (either sequential or simultaneous)

(2) Sequential oral auctions

(3) Simultaneous multiple round auctions

(b) The Commission may use combinatorial bidding, which would allow bidders to submit all or nothing bids on combinations of licenses, in addition to bids on individual licenses. The Commission may require that to be declared the high bid, a combinatorial bid must exceed the sum of the individual bids by a specified amount. Combinatorial bidding may be used with any type of auction.

(c) The Commission may use single combined auctions, which combine bidding for two or more substitutable licenses and award licenses to the highest bidders until the available licenses are exhausted. This technique may be used in conjunction with any type of auction.

§ 1.2104 Competitive Bidding Mechanisms

(a) *Sequencing.* The Commission will establish the sequence in which multiple licenses will be auctioned.

(b) *Grouping.* In the event the Commission uses either a simultaneous multiple round competitive bidding design or combinatorial bidding, the Commission will determine which licenses will be auctioned simultaneously or in combination.

(c) *Reservation Price.* The Commission may establish a reservation price, either disclosed or undisclosed, below which a license subject to auction will not be awarded.

(d) *Minimum Bid Increments.* The Commission may, by announcement before or during an auction, require minimum bid increments in dollar or percentage terms. The Commission may also establish suggested minimum opening bids on a service-specific basis.

(e) *Stopping Rules.* The Commission may establish stopping rules before or during multiple round auctions in order to terminate the auctions within a reasonable time.

(f) *Activity Rules.* The Commission may establish activity rules which require a minimum amount of bidding activity.

(g) *Withdrawal, Default and Disqualification Penalties.* As specified below, when the Commission conducts a simultaneous multiple round auction pursuant to § 1.2103, the Commission will impose penalties on bidders who withdraw high bids during the course of an auction, or who default on payments due after an auction closes or who are disqualified.

(1) Bid withdrawal prior to close of auction. A bidder who withdraws a high bid during the course of an auction will be subject to a penalty equal to the difference between the amount bid and the amount of the winning bid the next time the license is offered by the Commission. No withdrawal penalty would be assessed if the subsequent winning bid exceeds the withdrawn bid. This penalty amount will be deducted from any upfront payments or down payments that the withdrawing bidder has deposited with the Commission.

(2) Default or disqualification after close of auction. If a high bidder defaults or is disqualified after the close of such an auction, the defaulting bidder will be subject to the penalty in subsection (1) plus an additional penalty equal to 3 percent of the subsequent winning bid. If the subsequent winning bid exceeds the defaulting bidder's bid amount, the 3 percent penalty will be calculated based on the defaulting bidder's bid amount. These amounts will be deducted from any upfront payments or down payments that the defaulting or disqualified bidder has deposited with the Commission.

When the Commission conducts single round sealed bid auctions or sequential oral auctions, the Commission may modify the penalties to be paid in the event of bid withdrawal, default or disqualification; provided, however, that such penalties shall not exceed the penalties specified above.

(h) The Commission will generally release information concerning the identities of bidders before each auction but may choose, on an auction-by-auction basis, to withhold the identity of the bidders associated with bidder identification numbers.

(i) The Commission may delay, suspend, or cancel an auction in the event of a natural disaster, technical obstacle, evidence of security breach, unlawful bidding activity, administrative necessity, or for any other reason that affects the fair and efficient conduct of the competitive bidding. The Commission also has the authority, at its sole discretion, to resume the competitive bidding starting from the beginning of the current or some previous round or cancel the competitive bidding in its entirety.

§ 1.2105 Bidding Application and Certification Procedures; Prohibition of Collusion

(a) *Submission of Short Form Application (FCC Form 175).* In order to be eligible to bid, an applicant must timely submit a short-form application (FCC Form 175), together with any appropriate filing fee set forth by Public Notice. Unless otherwise provided by Public Notice, the Form 175 need not be accompanied by an upfront payment (*see* Section 1.2106 of this part).

(1) All Form 175s will be due:

(i) on the date(s) specified by Public Notice; or

(ii) in the case of application filing dates which occur automatically by operation of law (*see, e.g.,* 47 CFR Section 22.902), on a date specified by Public Notice after the Commission has reviewed the applications that have been filed on those dates and determined that mutual exclusivity exists.

(2) The Form 175 must contain the following information:

(i) Identification of each license on which the applicant wishes to bid;

(ii) The applicant's name, if the applicant is an individual. If the applicant is a corporation, then the short-form application will require the name and address of the corporate office and the name and title of an officer or director. If the applicant is a partnership, then the application will require the name, citizenship and address of all partners, and, if a partner is not a natural person, then the name and title of a responsible person should be included as well. If the applicant is a trust, then the name and address of the trustee will be required. If the applicant is none of the above, then it must identify and describe itself and its principals or other responsible persons;

(iii) The identity of the person(s) authorized to make or withdraw a bid;

(iv) If the applicant applies as a designated entity pursuant to § 1.2110 of these rules, a statement to that effect and a declaration, under penalty of perjury, that the applicant is qualified as a designated entity under § 1.2110 of the Commission's Rules;

(v) Certification that the applicant is legally, technically, financially and otherwise qualified pursuant to Section 308(b) of the Communications Act of 1934, as amended. The Commission will accept applications certifying that a request for waiver or other relief from the requirements of Section 310 is pending;

(vi) Certification that the applicant is in compliance with the foreign ownership provisions of Section 310 of the Communications Act of 1934, as amended;

(vii) Certification that the applicant is and will, during the pendency of its application(s), remain in compliance with any service-specific qualifications applicable to the licenses on which the applicant intends to bid including, but not limited to, financial qualifications. The Commission may require certification in certain services that the applicant will, following grant of a license, come into compliance with certain service-specific rules, including, but not limited to, ownership eligibility limitations;

(viii) An exhibit, certified as truthful under penalty of perjury, identifying all parties with whom the applicant has entered into partnerships, joint ventures, consortia or other agreements, arrangements or understandings of any kind relating to the licenses being auctioned, including any such agreements relating to the post-auction market structure.

(ix) Certification under penalty of perjury that it has not entered and will not enter into any explicit or implicit agreements, arrangements or understandings of any kind with any parties other than those identified pursuant to subsection (viii) regarding the amount of their bids, bidding strategies or the particular licenses on which they will or will not bid;

NOTE: The Commission may also request applicants to submit additional information for informational purposes to aid in its preparation of required reports to Congress.

(b) *Modification and Dismissal of Form 175.*

(1) Any Form 175 that is not signed or otherwise does not contain all of the certifications required pursuant to this section is unacceptable for filing and cannot be corrected subsequent to any applicable filing deadline. The application will be dismissed with prejudice and the upfront payment, if paid, will be returned.

(2) The Commission will provide bidders a limited opportunity to cure defects specified herein (except for failure to sign the application and to make certifications) and to resubmit a corrected application. Form 175 may be amended or modified to make minor changes or correct minor errors in the application (such as typographical errors). The Commission will classify all amendments as major or minor, pursuant to rules applicable to specific services. An application will be considered to be a newly filed application if it is amended by a major amendment and may not be resubmitted after applicable filing deadlines.

(3) Applicants who fail to correct defects in their applications in a timely manner as specified by Public Notice will have their applications dismissed with no opportunity for resubmission.

(c) *Prohibition of Collusion.*

(1) Except as provided in paragraphs (c)(2) and (c)(3) of this subsection, after the filing of short-form applications, all bidders are prohibited from cooperating, collaborating, discussing or disclosing in any manner the substance of their bids or bidding strategies, or discussing or negotiating settlement agreements, with other bidders until after the high bidder makes the required down payment, unless such bidders are members of a bidding consortium or other joint bidding arrangement identified on the bidder's short-form application pursuant to Section 1.2105(a)(2)(viii).

(2) Applicants may modify their short-form applications to reflect formation of consortia or changes in ownership at any time before or during an auction, provided such changes do not result in a change in control of the applicant, and provided that the parties forming consortia or entering into ownership agreements have not applied for licenses in any of the same geographic license areas. Such changes will not be considered major modifications of the application.

(3) After the filing of short-form applications, applicants may make agreements to bid jointly for licenses, provided the parties to the agreement have not applied for licenses in any of the same geographic license areas.

§ 1.2106 Submission of Upfront Payments

(a) The Commission may require applicants for licenses subject to competitive bidding to submit an upfront payment. In that event, the amount of the upfront payment and the procedures for submitting it will be set forth in a Public Notice. No interest will be paid on upfront payments.

(b) Upfront payments must be made either by wire transfer or by cashier's check drawn in U.S. dollars from a financial institution whose deposits are insured by the Federal Deposit Insurance Corporation and must be made payable to the Federal Communications Commission.

(c) If an upfront payment is not in compliance with the Commission's Rules, or if insufficient funds are tendered to constitute a valid upfront payment, the applicant shall have a limited opportunity to correct its submission to bring it up to the minimum valid upfront payment prior to the auction. If the applicant does not submit at least the minimum upfront payment, it will be ineligible to bid, its application will be dismissed and any upfront payment it has made will be returned.

(d) The upfront payment(s) of a bidder will be credited toward any down payment required for licenses on which the bidder is the high bidder. Where the upfront payment amount exceeds the required deposit of a winning bidder, the Commission may refund the excess amount after determining that no bid withdrawal penalties are owed by that bidder.

(e) In accordance with the provisions of subsection (d), in the event a penalty is assessed pursuant to § 1.2104 for bid withdrawal or default, upfront payments or down payments on deposit with the Commission will be used to satisfy the bid withdrawal or default penalty before being applied toward any additional payment obligations that the high bidder may have.

§ 1.2107 Submission of Down Payment and Filing of Long-Form Applications

(a) After bidding has ended, the Commission will identify and notify the high bidder and declare the bidding closed.

(b) Within five (5) business days after being notified that it is a high bidder on a particular license(s), a high bidder must submit to the Commission's lockbox bank such additional funds (the "down payment") as are necessary to bring its total deposits (not including upfront payments applied to satisfy penalties) up to twenty (20) percent of its high bid(s). (In single round sealed bid auctions conducted under § 1.2103, however, bidders may be required to submit their down payments with their bids.) This down payment must be made by wire transfer or cashier's check drawn in U.S. dollars from a financial institution whose deposits are insured by the Federal Deposit Insurance Corporation and must be made payable to the Federal Communications Commission. Winning bidders who are qualified designated entities eligible for installment payments under § 1.2110(d) are only required to bring their total deposits up to ten (10) percent of their winning bid(s). Such designated entities must pay the remainder of the twenty (20) percent down payment within five (5) business days of grant of their application. *See* § 1.2110(e)(1) and (2) of this subpart. Down payments will be held by the Commission until the high bidder has been awarded the license and has paid the remaining balance due on the license, in which case it will not be returned, or until the winning bidder is found unqualified to be a licensee or has defaulted, in which case it will be returned, less applicable penalties. No interest will be paid on any down payment.

(c) A high bidder that meets its down payment obligations in a timely manner must, within ten (10) business days after being notified that it is a high bidder, submit an additional application (the "long-form application") pursuant to the rules governing the service in which the applicant is the high bidder (unless it has already submitted such an application, as contemplated by §1.2105(a)(1)(b). For example, if the applicant is a high bidder for a license in the Interactive Video Data Service (*see* 47 CFR Part 95, Subpart F), the long form application will be submitted on FCC Form 574 in accordance with Section 95.815 of the Rules. Notwithstanding any other provision in Title 47 of the Code of Federal Regulations to the contrary, high bidders need not submit an additional application filing fee with their long-form applications. Notwithstanding any other provision in Title 47 of the Code of Federal Regulations to the contrary, the high bidder's long-form application must be mailed or otherwise delivered to:

Office of the Secretary
Federal Communications Commission
Attention: Auction Application Processing Section
1919 M Street, N.W., Room 222
Washington, D.C. 20554

An applicant that fails to submit the required long-form application as required under this subsection, and fails to establish good cause for any late-filed submission, shall be deemed to have defaulted and will be subject to the penalties set forth in § 1.2104 of the Commission's Rules.

(d) As an exhibit to its long-form application, the applicant must provide a detailed explanation of the terms and conditions and parties involved in any bidding consortia, joint venture, partnership or other agreement or arrangement it had entered into relating to the competitive bidding process prior to the time bidding was completed. Such agreements must have been entered into prior to the filing of short-form applications pursuant to § 1.2105.

§ 1.2108 Procedures for Filing Petitions To Deny Against Long-Form Applications

(a) Where petitions to deny are otherwise provided for under the Act or the Commission's Rules, and unless other service-specific procedures for the filing of such petitions are provided for elsewhere in the Commission's Rules, the procedures in this section shall apply to the filing of petitions to deny the long-form applications of winning bidders.

(b) Within thirty (30) days after the Commission gives public notice that a long-form application has been accepted for filing, petitions to deny that application may be filed. Any such petitions must contain allegations of fact supported by affidavit of a person or persons with personal knowledge thereof.

(c) An applicant may file an opposition to any petition to deny, and the petitioner a reply to such opposition. Allegations of fact or denials thereof must be supported by affidavit of a person or persons with personal knowledge thereof. The times for filing such opposition and replies will be those provided in § 1.45 of these Rules.

(d) If the Commission determines that:

(1) an applicant is qualified and there is no substantial and material issue of fact concerning that determination, it will grant the application.

(2) an applicant is not qualified and that there is no substantial issue of fact concerning that determination, the Commission need not hold an evidentiary hearing and will deny the application.

(3) substantial and material issues of fact require a hearing, it will conduct a hearing. The Commission may permit all or part of the evidence to be submitted in written form and may permit employees other than administrative law judges to preside at the taking of written evidence. Such hearing will be conducted on an expedited basis.

§ 1.2109 License Grant, Denial, Default, and Disqualification

(a) Unless otherwise specified in these rules, auction winners are required to pay the balance of their winning bids in a lump sum within five (5) business days following award of the license. Grant of the license will be conditioned on full and timely payment of the winning bid.

(b) If a winning bidder withdraws its bid after the Commission has declared competitive bidding closed or fails to remit the required down payment within five (5) business days after the Commission has declared competitive bidding closed, the bidder will be deemed to have defaulted, its application will be dismissed, and it will be liable for the default penalty specified in § 1.2104(g)(2). In such event, the Commission may either re-auction the license to existing or new applicants or offer it to the other highest bidders (in descending order) at their final bids. The down payment obligations set forth in § 1.2107(b) will apply.

(c) A winning bidder who is found unqualified to be a licensee, fails to remit the balance of its winning bid in a timely manner, or defaults or is disqualified for any reason after having made the required down payment, will be deemed to have defaulted and will be liable for the penalty set forth in § 1.2104(g)(2). In such event, the Commission will conduct another auction for the license, affording new parties an opportunity to file applications for the license.

(d) Bidders who are found to have violated the antitrust laws or the Commission's rules in connection with their participation in the competitive bidding process may be subject, in addition to any other applicable sanctions, to forfeiture of their upfront payment, down payment or full bid amount, and may be prohibited from participating in future auctions.

§ 1.2110 Designated Entities

(a) Designated entities are small businesses, businesses owned by members of minority groups and/or women, and rural telephone companies.

(b) Definitions.

(1) Small businesses. The Commission will establish the definition of a small business on a service-specific basis, taking into consideration the characteristics and capital Rrequirements of the particular service.

(2) Businesses owned by members of minority groups and/or women. Unless otherwise provided in rules governing specific services, a business owned by members of minority groups and/or women is one in which minorities and/or women who are U.S. citizens control the applicant, have at least 50.1 percent equity ownership and, in the case of a corporate applicant, a 50.1 percent voting interest. For applicants that are partnerships, every general partner either must be a minority and/or woman (or minorities and/or women) who are U.S. citizens and who individually or together own at least 50.1 percent of the partnership equity, or an entity that is 100 percent owned and controlled by minorities and/or women who are U.S. citizens. The interests of minorities and women are to be calculated on a fully-diluted basis; agreements such as stock options and convertible debentures shall be considered to have a present effect on the power to control an entity and shall be treated as if the rights thereunder already have been fully exercised. However, upon a demonstration that options or conversion rights held by non-controlling principals will not deprive the minority and female principals of a substantial financial stake in the venture or impair their rights to control the designated entity, a designated entity may seek a waiver of the requirement that the equity of the minority and female principals must be calculated on a fully-diluted basis. The term minority includes individuals of African American, Hispanic-surnamed, American Eskimo, Aleut, American Indian and Asian American extraction.

(3) Rural telephone companies. A rural telephone company is any local exchange carrier, including affiliates (as defined in 1.2110 (b)(4)), with 100,000 access lines or fewer.

(4) Affiliate. (1) An individual or entity is an *affiliate* of (a) an applicant or (b) a person holding an attributable interest in an applicant under § 24.709 (both referred to herein as "the applicant") if such individual or entity --

(i) directly or indirectly controls or has the power to control the applicant , or

(ii) is directly or indirectly controlled by the applicant, or

(iii) is directly or indirectly controlled by a third party or parties that also controls or has the power to control the applicant, or

(iv) has an "identity of interest" with the applicant.

(2) Nature of *control* in determining affiliation.

(i) Every business concern is considered to have one or more parties who directly or indirectly control or have the power Sto control it. Control may be affirmative or negative and it is immaterial whether it is exercised so long as the power to control exists.

Example. An applicant owning 50 percent of the voting stock of another concern would have negative power to control such concern since such party can block any action of the other stockholders. Also, the bylaws of a corporation may permit a stockholder with less than 50 percent of the voting stock to block any actions taken by the other stockholders in the other entity. Affiliation exists when the applicant has the power to control a concern while at the same time another person, or persons, are in control of the concern at the will of the party or parties with the power to control.

(ii) Control can arise through stock ownership; occupancy of director, officer or key employee positions; contractual or other business relations; or combinations of these and other factors. A key employee is an employee who, because of his/her position in the concern, has a critical influence in or substantive control over the operations or management of the concern.

(iii) Control can arise through management positions where a concern's voting stock is so widely distributed that no effective control can be established.

Example. In a corporation where the officers and directors own various size blocks of stock totaling 40 percent of the corporation's voting stock, but no officer or director has a block sufficient to give him or her control or the power to control and the remaining 60 percent is widely distributed with no individual stockholder having a stock interest greater than 10 percent, management has the pow-

er to control. If persons with such management control of the other entity are persons with attributable interests in the applicant, the other entity will be deemed an affiliate of the applicant.

(3) Identity of interest between and among persons. Affiliation can arise between or among two or more persons with an identity of interest, such as members of the same family or persons with common investments. In determining if the applicant controls or has the power to control a concern, persons with an identity of interest will be treated as though they were one person.

Example. Two shareholders in Corporation Y each have attributable interests in the same PCS application. While neither shareholder has enough shares to individually control Corporation Y, together they have the power to control Corporation Y. The two shareholders with these common investments (or identity in interest) are treated as though they are one person and Corporation Y would be deemed an affiliate of the applicant.

(i) Spousal Affiliation. Both spouses are deemed to own or control or have the power to control interests owned or controlled by either of them, unless they are subject to a legal separation recognized by a court of competent jurisdiction in the United States. In calculating their net worth, investors who are legally separated must include their share of interests in property held jointly with a spouse.

(ii) Kinship Affiliation. Immediate family members will be presumed to own or control or have the power to control interests owned or controlled by other immediate family members. In this context "immediate family member" means father, mother, husband, wife, son, daughter, brother, sister, father- or mother-in-law, son- or daughter-in-law, brother- or sister-in-law, step-father or -mother, step-brother or -sister, step-son or -daughter, half brother or sister. This presumption may be rebutted by showing that (A) the family members are estranged, (B) the family ties are remote, or (C) the family members are not closely involved with each other in business matters.

Example: A owns a controlling interest in Corporation X. A's sister-in-law, B, has an attributable interest in a PCS application. Because A and B have a presumptive kinship affiliation, A's interest in Corporation X is attributable to B, and thus to the applicant, unless B rebuts the presumption with the necessary showing.

(4) Affiliation through stock ownership.

(i) An applicant is presumed to control or have the power to control a concern if he or she owns or controls or has the power to control 50 percent or more of its voting stock.

(ii) An applicant is presumed to control or have the power to control a concern even though he or she owns, controls or has the power to control less than 50 percent of the concern's voting stock, if the block of stock he or she owns, controls or has the power to control is large as compared with any other outstanding block of stock.

(iii) If two or more persons each owns, controls or has the power to control less than 50 percent of the voting stock of a concern, such minority holdings are equal or approximately equal in size, and the aggregate of these minority holdings is large as compared with any other stock holding, the presumption arises that each one of these persons individually controls or has the power to control the concern; however, such presumption may be rebutted by a showing that such control or power to control, in fact, does not exist.

(5) Affiliation arising under stock options, convertible debentures, and agreements to merge. Stock options, convertible debentures, and agreements to merge (including agreements in principle) are generally considered to have a present effect on Uthe power to control the concern. Therefore, in making a size determination, such options, debentures, and agreements are generally treated as though the rights held thereunder had been exercised. However, an affiliate cannot use such options and debentures to appear to terminate its control over another concern before it actually does so.

Example 1. If company B holds an option to purchase a controlling interest in company A, who holds an attributable interest in a PCS application, the situation is treated as though company B had exercised its rights and had become owner of a controlling interest in company A. The gross revenues of company B must be taken into account in determining the size of the applicant.

Example 2. If a large company, BigCo, holds 70% (70 of 100 outstanding shares) of the voting stock of company A, who holds an attributable interest in a PCS application, and gives a third party, SmallCo, an option to purchase 50 of the 70 shares owned by BigCo, BigCo will be deemed to be an affiliate of company A, and thus the applicant, until SmallCo actually exercises its option to purchase such shares. In order to prevent BigCo from circumventing the intent of the rule which requires such options to be considered on a fully diluted basis, the option is not considered to have present effect in this case.

Example 3. If company A has entered into an agreement to merge with company B in the future, the situation is treated as though the merger has taken place.

(6) Affiliation under voting trusts.

(i) Stock interests held in trust shall be deemed controlled by any person who holds or shares the power to vote such stock, to any person who has the sole power to sell such stock, and to any person who has the right to revoke the trust at will or to replace the trustee at will.

(ii) If a trustee has a familial, personal or extra-trust business relationship to the grantor or the beneficiary, the stock interests held in trust will be deemed controlled by the grantor or beneficiary, as appropriate.

(iii) If the primary purpose of a voting trust, or similar agreement, is to separate voting power from beneficial ownership of voting stock for the purpose of shifting control of or the power to control a concern in order that such concern or another concern may meet the Commission's size standards, such

voting trust shall not be considered valid for this purpose regardless of whether it is or is not recognized within the appropriate jurisdiction.

(7) Affiliation through common management. Affiliation generally arises where officers, directors, or key employees serve as the majority or otherwise as the controlling element of the board of directors and/or the management of another entity.

(8) Affiliation through common facilities. Affiliation generally arises where one concern shares office space and/or employees and/or other facilities with another concern, particularly where such concerns are in the same or related industry or field of operations, or where such concerns were formerly affiliated, and through these sharing arrangements one concern has control, or potential control, of the other concern.

(9) Affiliation through contractual relationships. Affiliation generally arises where one concern is dependent upon another concern for contracts and business to such a degree that one concern has control, or potential control, of the other concern.

(10) Affiliation under joint venture arrangements.

(i) A joint venture for size determination purposes is an association of concerns and/or individuals, with interests in any degree or proportion, formed by contract, express or implied, to engage in and carry out a single, specific business venture for joint profit for which purpose they combine their efforts, property, money, skill and knowledge, but not on a continuing or permanent basis for conducting business generally. The determination whether an entity is a joint venture is based upon the facts of the business operation, regardless of how the business operation may be designated by the parties involved. An agreement to share profits/losses proportionate to each party's contribution to the business operation is a significant factor in determining whether the business operation is a joint venture.

(ii) The parties to a joint venture are considered to be affiliated with each other.

(c) The Commission may set aside specific licenses for which only eligible designated entities, as specified by the Commission, may bid.

(d) The Commission may permit partitioning of service areas in particular services for eligible designated entities.

(e) The Commission may permit small businesses (including small businesses owned by women, minorities, or rural telephone companies that qualify as small businesses) and other entities determined to be eligible on a service-specific basis, which are high bidders for licenses specified by the Commission, to pay the full amount of their high bids in installments over the term of their licenses pursuant to the following:

(1) Unless otherwise specified, each eligible applicant paying Wfor its license(s) on an installment basis must deposit by wire transfer or cashier's check in the manner specified in § 1.2107(b) sufficient additional funds as are necessary to bring its total deposits to ten (10) percent of its winning bid(s) within five (5) business days after the Commission has declared it the winning bidder and closed the bidding. Failure to remit the required payment will make the bidder liable to pay penalties pursuant to § 1.2104(g)(2).

(2) Within five (5) business days of the grant of the license application of a winning bidder eligible for installment payments, the licensee shall pay another ten (10) percent of the high bid, thereby commencing the eligible licensee's installment payment plan. Failure to remit the required payment will make the bidder liable to pay penalties pursuant to § 1.2104(g)(2).

(3) Upon grant of the license, the Commission will notify each eligible licensee of the terms of its installment payment plan. Unless other terms are specified in the rules of particular services, such plans will:

(i) impose interest based on the rate of U.S. Treasury obligations (with maturities closest to the duration of the license term) at the time of licensing;

(ii) allow installment payments for the full license term;

(iii) begin with interest-only payments for the first two years; and

(iv) amortize principal and interest over the remaining term of the license.

(4) A license granted to an eligible entity that elects installment payments shall be conditioned upon the full and timely performance of the licensee's payment obligations under the installment plan.

(i) If an eligible entity making installment payments is more than ninety (90) days delinquent in any payment, it shall be in default.

(ii) Upon default or in anticipation of default of one or more installment payments, a licensee may request that the Commission permit a three to six month grace period, during which no installment payments need be made. In considering whether to grant a request for a grace period, the Commission may consider, among other things, the licensee's payment history, including whether the licensee has defaulted before, how far into the license term the default occurs, the reasons for default, whether the licensee has met construction build-out requirements, the licensee's financial condition, and whether the licensee is seeking a buyer under an authorized distress sale policy. If the Commission grants a request for a grace period, or otherwise approves a restructured payment schedule, interest will continue to accrue and will be amortized over the remaining term of the license.

(iii) Following expiration of any grace period without successful resumption of payment or upon denial of a grace period request, or upon default with no such request submitted, the license will automatically cancel and the Commission will initiate debt collection procedures pursuant to Part 1, Subpart O of the Commission's Rules.

(e) The Commission may award bidding credits (*i.e.*, payment discounts) to eligible designated entities. Competitive bidding rules applicable to individual services will

specify the designated entities eligible for bidding credits, the licenses for which bidding credits are available, the amounts of bidding credits and other procedures.

(f) The Commission may establish different upfront payment requirements for categories of designated entities in competitive bidding rules of particular auctionable services.

(g) The Commission may offer designated entities a combination of the available preferences or additional preferences.

(h) Designated entities must describe on their long-form applications how they satisfy the requirements for eligibility for designated entity status, and must list and summarize on their long-form applications all agreements that effect designated entity status, such as partnership agreements, shareholder agreements, management agreements and other agreements, including oral agreements, which establish that the designated entity will have both *de facto* and *de jure* control of the entity. Such information must be maintained at the licensees' facilities or by their designated agents for the term of the license in order to enable the Commission to audit designated entity eligibility on an ongoing basis.

(i) The Commission may, on a service-specific basis, permit consortia, each member of which individually meets the eligibility requirements, to qualify for any designated entity provisions.

(j) The Commission may, on a service-specific basis, permit publicly-traded companies that are owned by members of minority groups or women to qualify for any designated entity provisions.

§ 1.2111 Assignment or transfer of control: unjust enrichment

(a) *Reporting requirement.* An applicant seeking approval for a transfer of control or assignment (otherwise permitted under the Commission's Rules) of a license within three years of receiving a new license through a competitive bidding procedure must, together with its application for transfer of control or assignment, file with the Commission a statement indicating that its license was obtained through competitive bidding. Such applicant must also file with the Commission the associated contracts for sale, option agreements, management agreements, or other documents disclosing the total consideration that the applicant would receive in return for the transfer or assignment of its license. This information should include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (*e.g.,* management or consulting contracts either with or without an option to purchase; below market financing).

(b) *Unjust enrichment payment: set-asides.* As specified in this subsection, an applicant seeking approval for a transfer of control or assignment (otherwise permitted under the Commission's Rules) of a license acquired by the transferor or assignor pursuant to a set-aside for eligible designated entities under § 1.2110(c) of the Commission's Rules, or who proposes to take any other action relating to ownership or control that will result in loss of status as an eligible designated entity, must seek Commission approval and may be required to make an unjust enrichment payment (Payment) to the Commission by cashier's check or wire transfer before consent will be granted. The Payment will be based upon a schedule that will take account of the term of the license, any applicable construction benchmarks, and the estimated value of the set-aside benefit, which will be calculated as the difference between the amount paid by the designated entity for the license and the value of a comparable non-set-aside license in the free market at the time of the auction. The Commission will establish the amount of the Payment and the burden will be on the applicants to disprove this amount. No Payment will be required if:

(1) the license is transferred or assigned more than five years after its initial issuance, unless otherwise specified; or

(2) the proposed transferee or assignee is an eligible designated entity under § 1.2110(c) of the Commission's Rules or the service-specific competitive bidding rules of the particular service, and so certifies.

(c) *Unjust enrichment payment: installment financing.* An applicant seeking approval for a transfer of control or assignment (otherwise permitted under the Commission's Rules) of a license acquired by the transferor or assignor through a competitive bidding procedure utilizing installment financing available to designated entities under § 1.2110(d) of the Rules will be required to pay the full amount of the remaining principal balance as a condition of the license transfer. No payment will be required if the proposed transferee or assignee assumes the installment payment obligations of the transferor or assignor, and if the proposed transferee or assignee is itself qualified to obtain installment financing under § 1.2110(d) of the Rules or the service-specific competitive bidding rules of the particular service, and so certifies.

(d) *Unjust enrichment payment: bidding credits.* An applicant seeking approval for a transfer of control or assignment (otherwise permitted under the Commission's Rules) of a license acquired by the transferor or assignor through a competitive bidding procedure utilizing bidding credits available to eligible designated entities under § 1.2110(e) of the Rules, or who proposes to take any other action relating to ownership or control that will result in loss of status as an eligible designated entity, must seek Commission approval and will be required to make an unjust enrichment payment (Payment) to the government by wire transfer or cashier's check before consent will be granted. The Payment will be the sum of the amount of the bidding credit plus interest at the rate applicable for installment financing in effect at the time the license was awarded. *See* § 1.2110(e). No payment will be required if the proposed transferee or assignee is an eligible designated entity under § 1.2110(e) of the Commission's Rules or the service-specific competitive bidding rules of the particular service, and so certifies.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

STAR CABLE ASSOCIATES

Petition for Reconsideration

of the Certification of
St. Martin Parish, Louisiana
to Regulate Basic Cable Rates
(LA0551)

MEMORANDUM OPINION AND ORDER

Adopted: November 28, 1994; Released: November 29, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On December 13, 1993, Star Cable Associates ("Star Cable") filed a timely petition for reconsideration challenging the certification of St. Martin Parish Police Jury to regulate rates for basic cable service and associated equipment in St. Martin Parish, Louisiana.[1] St. Martin Parish did not file an opposition to Star Cable's petition.

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[2] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[3] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[4] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[5] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[6]

II. DISCUSSION

3. Star Cable argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in the unincorporated areas of St. Martin Parish, its franchise area.[7] Star Cable claims that it currently serves only 83 of the 9,256 households (that is, occupied housing units)[8] in its franchise area, or less than one percent of the total number of households. As supporting documentation, Star Cable provides 1990 Census data[9] which shows that there are 9,256 households in the unincorporated areas of St. Martin Parish. Star Cable also submits a computer print-out with sufficient subscriber information to support its claim that it serves 83 households in the franchise area. Finally, Star Cable provides an affidavit by a responsible official certifying the accuracy of the data included in the petition.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[10] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[11] Star Cable has met this burden. Star Cable appropriately relied on data reflecting the number of households as required by our rules.[12] Relying on this data, Star Cable has submitted sufficient evidence demonstrating that its cable system serving St. Martin Parish, its franchise area, serves 83 of the 9,256 households, or less than one percent of the households, within its franchise area. Thus, we find Star Cable's system serving St. Martin Parish is subject to effective competition. Accordingly, its petition is granted.

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[1] St. Martin Parish filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on October 19, 1993, which became effective on November 18, 1993.

[2] 47 U.S.C. § 543(a)(4).

[3] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[4] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition. 47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[5] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[6] 47 C.F.R. § 76.911(c).

[7] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[8] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*"Third Recon. Order"*). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[9] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994).

[10] 47 C.F.R. § 76.906.

[11] 47 C.F.R. § 76.911(b)(1).

[12] *Third Recon. Order, supra.*

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Star Cable challenging the certification of St. Martin Parish Police Jury to regulate basic cable rates IS GRANTED.

6. IT IS FURTHER ORDERED that the certification of St. Martin Parish Police Jury to regulate Star Cable's basic cable rates IS RESCINDED.

7. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

FEDERAL COMMUNICATIONS COMMISSION

Before the
Federal Communications Commission
Washington, D.C. 20554

PUBLIC NOTICE

Released: November 30, 1994

PLEADING CYCLE ESTABLISHED FOR COMMENTS ON BELL ATLANTIC'S PETITION FOR WAIVER OF PART 69 RULES TO OFFER VIDEO DIALTONE SERVICE

On November 29, 1994, Bell Atlantic Telephone Companies (Bell Atlantic) filed a petition seeking an expedited waiver of the Commission's rules in order to establish a new rate structure and tariff rate elements for video dialtone service under transport categories of Part 69. Bell Atlantic states that a waiver is necessary for it to file a tariff offering video dialtone service. Bell Atlantic proposes to establish recurring and non-recurring charges to be assessed to programmer-customers or end-user subscribers for video dialtone service components because a uniform rate structure is not currently prescribed for video dialtone service.

Specifically, Bell Atlantic requests a waiver of Parts 69.110 and 69.112 to allow establishment of the video dialtone rate structure. Bell Atlantic states that the revenues from video dialtone rates and charges will be included with other transport revenues. Bell Atlantic also requests a waiver of Part 69.305 to allow video dialtone investment included in Cable and Wire Facilities Category 2 to be directly assigned to the Transport Part 69 elements. In addition, Bell Atlantic requests a waiver under Part 69.307(c) of the rules to assign general support facilities used in the provision of video dialtone services to be directly assigned to the Transport elements. Bell Atlantic urges the Commission to act expeditiously on its waiver request so that it may provide customers with video dialtone service at the earliest possible date.

Interested parties should file comments on Bell Atlantic's petition by **December 9, 1994**, and reply comments by **December 14, 1994**, with the Secretary, FCC, 1919 M Street, N.W., Washington, D.C. 20554. A copy should also be sent to Peggy Reitzel, Common Carrier Bureau, FCC, Room 544, 1919 M Street, N.W., Washington, D.C. 20554, and to the Commission's contractor for public service records duplication: ITS, Inc. 2100 M Street, N.W., Suite 140, Washington, D.C. 20037. Bell Atlantic's petition is available for inspection and copying in the Policy and Program Planning Division, Common Carrier Bureau, Room 544, 1919 M Street, N.W., Washington, D.C. 20554. Copies also can be obtained from ITS at (202) 857-3800.

We will treat this proceeding as non-restricted for purposes of the Commission's *ex parte* rules. *See generally* 47 C.F.R. §§ 1.1200-1.1216. For further information contact Peggy Reitzel, Policy and Program Planning Division of the Common Carrier Bureau, at (202) 632-1300.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Delegation of Authority in
Forfeiture Proceedings

ORDER

Adopted: November 21, 1994; Released: December 8, 1994

By the Chief, Compliance and Information Bureau:[1]

1. By Order adopted and released on May 11, 1992, the Chief, Field Operations Bureau (now the Compliance and Information Bureau), delegated authority to the Chief, Enforcement Division, Field Operations Bureau, to impose forfeitures in amounts up to and including $20,000. *See* 47 C.F.R. § 0.311 (d)(1). The Chief, Enforcement Division, is responsible for developing and carrying out the agency's enforcement plan and administering all activities necessary to do so. This includes overseeing the Bureau's forfeiture proceedings.

2. The purpose of this *Order* is to specify that, the Chief, Enforcement Division, has authority to issue orders cancelling forfeitures in response to petitions for reconsideration filed pursuant to section 1.106 of the Commission's rules, 47 C.F.R. § 1.106. *See* 47 C.F.R. § 0.311 (d)(1).

3. Accordingly, IT IS ORDERED that the Chief, Enforcement Division, Compliance and Information Bureau, IS DELEGATED authority to issue orders cancelling forfeitures in response to petitions for reconsideration filed pursuant to section 1.106 of the Commission's rules, 47 C.F.R. § 1.106.

FEDERAL COMMUNICATIONS COMMISSION

Beverly G. Baker
Chief, Compliance and Information Bureau

[1] As a result of letters, dated October 20, 1994, sent by the Commission to Appropriate House and Senate Subcommittees, there were no Congressional objections to changing the name of Field Operations Bureau to the Compliance and Information Bureau. This name change is effective November 27, 1994.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Cable & Wireless, Inc. — File No. I-T-C-93-328

Application for Authority Under Section 214 of the Communications Act to Resell International Private Lines Interconnected into the Public Switched Network between the United States and Canada, the United Kingdom, Australia, and Sweden.

MEMORANDUM OPINION, ORDER AND AUTHORIZATION

Adopted: November 18, 1994; Released: December 8, 1994

By the Chief, Telecommunications Division:

I. INTRODUCTION

1. On September 9, 1993, Cable and Wireless, Inc. (CWI) filed the above-captioned application seeking authority pursuant to Section 214 of the Communications Act (the Act), as amended, to resell international private lines interconnected at both ends to the public switched network (PSN) for the provision of switched services, including switched voice, data and facsimile, between the United States and Canada, the United Kingdom, Australia and Sweden.

II. BACKGROUND

2. We placed the application on public notice on September 22, 1993. AT&T and Sprint each filed a petition to deny. FGC, Inc. (FGC) filed comments in support of CWI's application. Telia AB (Telia) and IDB Communications Group, Inc. (IDB) also filed comments.[1] In response to the petitions to deny and comments, CWI filed an opposition to the petitions to deny and reply comments. AT&T, British Telecom (BT), Sprint, FGC, and Telstra Corporation Limited (Telstra)[2] then responded to CWI's pleadings.[3]

3. In this order, we act only on the portion of CWI's application for authority to resell international private lines for the provision of switched services between the United States and the United Kingdom.[4] Accordingly, we address below the parties' arguments relevant to that specific portion of CWI's application. We defer action on the remaining portions of CWI's application (resale of international private lines for the provision of switched services between the United States and Australia and between the United States and Sweden).

III. DISCUSSION

4. The Commission has previously concluded that the public interest in cost-based telecommunications services would be served by international private line resale, which should, *inter alia*, exert downward pressure on high, above-cost international accounting rates. To ensure that such resale does not exacerbate the U.S. net settlements deficit, the Commission has conditioned its resale policy by requiring U.S. carriers to permit resale of their international private lines only to those countries that afford resale opportunities equivalent to those available in the United States.[5] The Commission requires that, at a minimum, the destination country afford open entry for, and nondiscriminatory treatment of, U.S.-based carriers, as well as the opportunity to interconnect the international private line at both ends of the circuit. The Commission may also consider other terms and conditions surrounding the resale of international private lines in the destination country. On September 19, 1994, the Commission determined that equivalent international private line resale opportunities exist in the United Kingdom for U.S.-based carriers seeking to provide service between the United States and the United Kingdom.[6]

5. IDB states that CWI should not be subject to the Commission's equivalency requirement because it applies only to international private line resale. IDB asserts that CWI's application should be treated as a request for authority to operate as a facilities-based carrier because the CWI's application states that CWI proposes to lease the

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[1] Until July 1, 1993, Telia was a government-owned telecommunications provider in Sweden, known as "Televerket, the Swedish Telecom Group". The Swedish Parliament separated the operational and regulatory functions of Televerket, and thus Telia, a limited commercial company, was formed to carry out the operational functions. Telia limited its comments to a discussion regarding the Swedish telecommunications market.

[2] Telstra is a government-owned telecommunications provider in Australia, and is one of two "General Carriers" licensed by the Australian Ministry for Transport and Communications. Telstra limited its comments to a discussion of the telecommunications market in Australia.

[3] Subsequently, in a letter dated March 9, 1994, CWI stated that it would not object to partial consideration of and action on the instant application, with deferral to a later date of those issues left unresolved *See* Letter from Charles A. Tievsky, Regulatory Attorney, CWI to George S. Li, Chief, International Facilities Division, Common Carrier Bureau, FCC (March 9, 1994). No comments were received with respect to CWI's letter.

[4] On November 2, 1994 we granted CWI that portion of its application requesting authorization to serve Canada, and deferred consideration of the rest of the application. In that authorization, we indicated that we would next turn to CWI's request for authorization to serve the United Kingdom. *See CWI* Authorization, File No. I-T-C-93-328, DA 94-1227 (Int. Bur., released November 2, 1994).

[5] *See* Regulation of International Accounting rates, CC Docket 90-337, Phase II, First Report and Order, 7 FCC Rcd 559 (1992). *See also* Regulation of International Accounting Rates, CC Docket 90-337, Phase II Order on Reconsideration and Third Further Notice of Proposed Rulemaking, 7 FCC Rcd 7927 (1992).

[6] *ACC Global Corporation and Alanna Inc.*, FCC 94-236, released October 6, 1994.

underlying transmission facilities from U.S. carriers.[7] By letter dated July 27, 1994, CWI clarified that it proposed to resell the international private line services of AT&T, MCI, Sprint and IDB pursuant to their filed and effective FCC tariffs, and/or pursuant to negotiated contracts with authorized international carriers.[8] CWI's application is thus considered resale and subject to the Commission's equivalency requirement.

6. Both AT&T and Sprint oppose grant of CWI's application for resale of international private lines for switched services between the United States and the United Kingdom based on arguments that the United Kingdom does not afford equivalent resale opportunities. As noted above, during the pendency of this proceeding the Commission has determined that the United Kingdom affords resale opportunities equivalent to those available under U.S. law,[9] thus rendering these arguments moot.

7. Independent of whether the U.K. offers equivalent resale opportunities for U.S.-based carriers, AT&T asserts that the Commission should apply a comparable market access standard to CWI's resale application, and that CWI, as a foreign-based carrier, should not be allowed entry to the U.S. telecommunications market pursuant to that standard. Specifically, AT&T argues that U.S. carriers do not have comparable opportunities to compete in the foreign telecommunication markets where CWI has monopoly and duopoly positions for the provision of telecommunications services.

8. In the past, the Commission has examined applications filed by foreign carriers on a case-by-case basis, balancing our policy in favor of open entry against the potential for discrimination by a foreign carrier against unaffiliated U.S. carriers.[10] Following this approach, we have previously authorized CWI and BT North America, a wholly-owned subsidiary of British Telecommunications, plc., to provide resold switched and non-interconnected private line services to various countries.[11] We have also granted CWI authority to resell international private lines interconnected at both ends to Canada, as well as to provide facilities-based private line service to Canada.[12] The Commission has not to date adopted a policy of requiring comparable market access as a condition of entry by foreign carriers on either a resale or facilities ownership basis. Indeed, we have granted many authorizations for resale in particular because resellers offer significant benefits to consumers in terms of lower costs and innovative services, while raising fewer concerns about anticompetitive conduct because they do not control the underlying transmission facilities.

9. We note that AT&T has filed a petition for rulemaking on the issue of foreign carrier entry in which it urges us to adopt a comparable market access standard for both facilities-based and resale service.[13] There may indeed be a need to take a comprehensive look at how we evaluate foreign carrier entry into the U.S. telecommunications market. We consider, however, that the development and application of market access standards would be a broad policy change appropriately done in a rulemaking proceeding, not in an individual Section 214 proceeding. We thus evaluate this application in accordance with existing Commission precedent.

10. We also note that, even if we were to consider foreign market access in determining whether the public interest would be served by the partial grant of this application, U.K. regulatory and market conditions for U.S.-based carriers seeking to resell international private lines for switched services would likely weigh in favor of the applicant. In the context of international private line resale applications filed by two U.S. carriers, ACC Global Corp. and Alanna Inc., the Commission has recently undertaken an in-depth review of U.K. regulatory and market conditions, including those issues raised by AT&T in its comments. Based on that review, the Commission determined that the United Kingdom affords U.S.-based carriers opportunities to resell private lines to provide switched services equivalent to those available under U.S. law.

11. More specifically, the U.K. permits any party to resell IMTS as well as non-interconnected or one-end interconnected private lines without any prior U.K. government authorization under an existing class license -- the U.K. Telecommunication Services License. It is also noteworthy that the U.K. telecommunications market is one of the most liberalized in the world, and certainly the most liberalized in the European Union. In fact the United Kingdom has few regulatory barriers to entry and has no foreign ownership limitations. The United Kingdom permits competition in all services, with the significant exception of international facilities-based services. As the Commission has noted previously, the U.K. government has taken considerable steps toward creating a regulatory regime under which effective competition to BT is likely to emerge, particularly with regard to the interconnection and access deficit contribution regimes. Examples of the openness of the U.K. telecommunications market include the Department of Trade and Industry's recent grant of several domestic facilities-based and international simple resale licenses to U.S. carriers, including Sprint, WorldCom, MFS Inc., ACC Global Corp., and City of London Telecommunications (COLT). In addition, the U.K. government has also announced its intent to grant AT&T's pending license. Finally, we note that U.S. carriers, such as U S West and NYNEX, are licensed in the United Kingdom as cable operators, and as such are also providing telephony.

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[7] Subsequent to filing its comments in this proceeding, IDB filed a petition for rulemaking asking the Commission to adopt a uniform definition of facilities-based carrier for purposes of Commission rules and policies governing international common carriers. *See* RM 8392 (filed October 29, 1993) (*see* Public Notice of November 30, 1993).

[8] *See* Letter from Charles A. Tievsky, Senior Regulatory Attorney, CWI to Jennifer Warren, Esquire, FCC (July 27, 1994).

[9] *See* note 6, *supra*.

[10] *AmericaTel Corporation*, 9 FCC Rcd 3993, 3996 (1994) (citing *Telefonica Larga Distancia de Puerto Rico*, 8 FCC Rcd 107, 108 (1992)). *See also fONOROLA/EMI*, 7 FCC Rcd 7312 (1992), *order on recon.*, 9 FCC Rcd 4066 (1994).

[11] *See e.g.*, CWI Authorization, 8 FCC Rcd 1664 (Com. Car. Bur. 1993) and CWI authorization, 7 FCC Rcd 4384 (Com. Car. Bur. 1992), *Order on Clarification*, DA 94-1132, (released October 21, 1994.)

[12] *See* note 4, *supra*.

[13] *See* AT&T's *Petition for rulemaking on market entry and regulation of international common carriers with foreign carrier affiliations*, RM-8355 (filed September 22, 1993) (*see* Public Notice of October 1, 1993).

12. AT&T further argues that CWI's entry into the international private line resale market should be conditioned upon implementation of cost-based, nondiscriminatory accounting rates on the U.S. - U.K. route. In the *International Resale Order,* the Commission expressly stated that one benefit expected from permitting international private line resale between equivalent countries would be the exertion of a downward pressure on above-cost accounting rates. We accordingly did not require cost-based accounting rates as a precondition to international private line resale. We, nonetheless, recognize that, where the Section 214 international private line resale applicant is affiliated with a foreign carrier that is either a facilities-based monopolist (or part of a facilities-based duopoly) on the foreign end, it is not as clear what the impact will be on the foreign carrier's willingness to negotiate lower accounting rates with U.S. facilities-based carriers. We note that AT&T has asked us to examine this issue in the context of its pending petition for rulemaking on foreign carrier entry.[14] We believe that this issue also is more appropriately addressed in a rulemaking proceeding than in individual Section 214 applications.

13. As a result of the Commission's equivalency finding for the United Kingdom, resale of interconnected international private lines for the provision of switched and private line services between the United States and the United Kingdom is permitted subject to grant of appropriate Section 214 authorization. We find that the present and future public convenience and necessity require the grant of this authorization to CWI.

14. We note that CWI also requests classification as a nondominant carrier on the U.S. - U.K. route. In this instance, CWI is ultimately wholly-owned by Cable & Wireless plc. (C&W plc.), a U.K. corporation, which owns an 80% equity interest in Mercury Communications Ltd. (Mercury). Mercury is one of only two authorized international facilities-based service providers in the United Kingdom. In addition, Mercury provides a full range of domestic facilities-based services in the United Kingdom. We believe that the affiliation between CWI and Mercury in the United Kingdom requires that we give greater scrutiny to the appropriate regulatory status for CWI on the U.S.-U.K. route.[15] In order not to delay unnecessarily CWI's authorization to initiate service, we defer consideration of CWI's request for nondominance on this route to a later date, and will continue to regulate CWI as dominant for the service authorized in this order.

15. Accordingly, IT IS ORDERED that application File No. I-T-C-93-328 IS GRANTED IN PART, and DEFERRED IN PART, and CWI is authorized to resell international private lines for the provision of switched services between the United States and the United Kingdom.

16. IT IS FURTHER ORDERED that AT&T's Petition to Deny IS DENIED IN PART and DEFERRED IN PART; and that Sprint's Petition to Deny in Part is DENIED IN PART AND DEFERRED IN PART.

17. IT IS FURTHER ORDERED that CWI is authorized to lease and operate up to 25 E-1 circuits from authorized U.S. carriers[16] for the provision of its authorized resale of international private lines.

18. IT IS FURTHER ORDERED that:

(a) CWI shall file publicly any contracts entered into with other carriers or a contract summary in accordance with Section 203 of the Communications Act, 47 U.S.C. §203, and the *Interexchange Order*;[17]

(b) CWI shall not agree to accept from such other carriers any services that are not made generally available by those carriers to similarly situated customers at the same terms, conditions and rates; and

(c) CWI shall file tariff provisions pursuant to Section 203 of the Communications Act, 47 U.S.C. §203, and Part 61 of the Commission's Rules, 47 C.F.R. Part 61, for the services authorized in this Order.

19. IT IS FURTHER ORDERED that the authority granted herein to resell international private lines for the provision of switched services between the United States and the United Kingdom is limited to the provision of such services between the United States and the United Kingdom only--that is, private lines which carry traffic that originates in the United States and terminates in the United Kingdom, or traffic that originates in the United Kingdom and terminates in the United States.

20. IT IS FURTHER ORDERED that neither CWI nor any person or companies directly or indirectly controlling it or controlled by it, or under direct or indirect common control with it, shall acquire or enjoy any right, for the purposes of handling or interchanging traffic to or from the United States, its territories or possessions which is denied to any other United States carrier by reason of any concession, contract, understanding, or working arrangement to which CWI or any such persons or companies controlling or controlled by CWI are parties.

21. IT IS FURTHER ORDERED that CWI shall comply with the requirements of Sections 43.51(a), 43.61 and 63.14 of the Commission's Rules, 47 C.F.R. §§ 43.51(a), 43.61 and 63.14.

22. IT IS FURTHER ORDERED that CWI shall file with the Commission within thirty (30) days of execution a copy of any operating agreement it enters into with its foreign correspondents; and that it shall also file with the Commission within 30 days of execution copies of any operating agreements entered into by its parent/affiliates that affect traffic or revenue flows between the United States and Canada; and that it shall otherwise comply with the filing requirements contained in Section 43.51 of the Commission's Rules, 47 C.F.R. Section 43.51.

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[14] *See* note 12, *supra*. *See also* AT&T Petition to Deny filed on the BT North America Section 214 Application, File No. I-T-C-93-126.

[15] *See also* CWI Authorization, File No. I-T-C-94-328, DA 94-1227 (Int. Bur., released November 4, 1994) (deferring nondominance for international private line resale to Canada to examine further the implications of a 20 percent stake in CWI's U.K. affiliate, Mercury, by Bell Canada Enterprises) (*citing* Memorandum Opinion and Order, File No. ISP-93-007-ND, DA 94-1134 (Com. Car. Bur., released October 21, 1994) and Memorandum Opinion and Order, File No. ISP-93-006-ND, DA 94-1133 (Com. Car. Bur., released October 21, 1994)).

[16] Initially, CWI intends to resell the private lines of one or more of the following carriers pursuant to contract or tariff: AT&T Tariff FCC No. 9, Sprint Tariff FCC No. 7, MCI/WUI Tariff FCC No. 27, and IDB Tariff FCC No. 2.

[17] *See Competition in the Interstate Interexchange Marketplace,* 6 FCC Rcd 5880, 5902 (1991) (*Interexchange Order*).

23. IT IS FURTHER ORDERED that CWI, as a dominant carrier, shall request Section 214 authorization for all circuit additions to Canada pursuant to Section 63.01 of the Rules, 47 C.F.R. §63.01.

24. IT IS FURTHER ORDERED that CWI, as a dominant carrier, shall file quarterly reports of revenue, number of messages, and number of minutes of both originating and terminating traffic for all international services between the United States and Canada within 90 days from the end of each calendar quarter.

25. IT IS FURTHER ORDERED that this order may be subject to future modification or revocation pursuant to the outcome of any relevant proceedings of general applicability.

26. IT IS FURTHER ORDERED that grant of this authorization to resell international private lines for the provision of switched services between the United States and the United Kingdom is conditioned upon the United Kingdom's continuing to afford resale opportunities equivalent to those available under U.S. law.

27. This Order is issued under Section 0.261 of the Commission's Rules and is effective upon adoption. Petitions for reconsideration under Section 1.106 or applications for review under Section 1.115 of the Commission's Rules may be filed within 30 days of the public notice of this Order (*see* Section 1.4(b)(2)).

FEDERAL COMMUNICATIONS COMMISSION

Diane J. Cornell
Chief, Telecommunications Division
International Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-142

In the Matter of

Amendment of Section 73.202(b), RM-8546
Table of Allotments,
FM Broadcast Stations.
(Knoxville, Illinois)

NOTICE OF PROPOSED RULE MAKING

Adopted: November 29, 1994; Released: December 8, 1994

Comment Date: January 30, 1995
Reply Comment Date: February 14, 1995

By the Acting Chief, Allocations Branch:

1. The Commission has before it the petition for rule making filed by John Pritchard ("petitioner"), proposing the allotment of Channel 287A to Knoxville, Illinois, as that community's first local transmission service. Petitioner states his intention to apply for the channel, if allotted.

2. We believe the public interest would be served by proposing the allotment of Channel 287A to Knoxville, Illinois, since it could provide the community with its first local transmission service. An engineering analysis had determined that Channel 287A can be allotted to Knoxville in compliance with the Commission's minimum distance separation requirements without a site restriction.[1]

3. The Commission believes it would be in the public interest to seek comments on the proposal to amend the FM Table of Allotments, Section 73.202(b) of the Commission's Rules, with respect to the following community:

	Channel No.	
City	Present	Proposed
Knoxville, Illinois		287A

4. The Commission's authority to institute rule making proceedings, showings required, cut-off procedures, and filing requirements are contained in the attached Appendix and are incorporated by reference herein. In particular, we note that a showing of continuing interest is required by paragraph 2 of the Appendix before a channel will be allotted.

5. Interested parties may file comments on or before **Jaunary 30, 1995**, and reply comments on or before **February 14, 1995**, and are advised to read the Appendix for the proper procedures. Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554. Additionally, a copy of such comments should be served on the petitioner, or its counsel or consultant, as follows:

Donald E. Ward
1201 Pennsylvania Avenue, N.W.
5th Floor
Washington, D.C. 20004
(Attorney for Petitioner)

6. The Commission has determined that the relevant provisions of the Regulatory Flexibility Act of 1980 do not apply to rule making proceedings to amend the FM Table of Allotments, Section 73.202(b) of the Commission's Rules. See *Certification that Sections 603 and 604 of the Regulatory Flexibility Act Do Not Apply to Rule Making to Amend Sections 73.202(b), 73.504 and 73.606(b) of the Commission's Rules*, 46 FR 11549, February 9, 1981.

7. For further information concerning this proceeding, contact Nancy J. Walls, Mass Media Bureau, (202) 634-6530. For purposes of this restricted notice and comment rule making proceeding, members of the public are advised that no *ex parte* presentations are permitted from the time the Commission adopts a Notice of Proposed Rule Making until the proceeding has been decided and such decision is no longer subject to reconsideration by the Commission or review by any court. An *ex parte* presentation is not prohibited if specifically requested by the Commission or staff for the clarification or adduction of evidence or resolution of issues in the proceeding. However, any new written information elicited from such a request or a summary of any new oral information shall be served by the person making the presentation upon the other parties to the proceeding unless the Commission specifically waives this service requirement. Any comment which has not been served on the petitioner constitutes an *ex parte* presentation and shall not be considered in the proceeding. Any reply comment which has not been served on the person(s) who filed the comment, to which the reply is directed, constitutes an *ex parte* presentation and shall not be considered in the proceeding.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

APPENDIX

1. Pursuant to authority found in Sections 4(i), 5(c)(1),303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61 0.204(b) and 0.283 of the Commission's Rules, IT IS PROPOSED TO AMEND the FM Table of Allotments, Section 73.202(b) of

[1] The coordinates for Channel 287A at Knoxville are North Latitude 40-54-30 and West Longitude 90-16-54.

the Commission's Rules and Regulations, as set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached.

2. *Showings Required.* Comments are invited on the proposal(s) discussed in the *Notice of Proposed Rule Making* to which this Appendix is attached. Proponent(s) will be expected to answer whatever questions are presented in initial comments. The proponent of a proposed allotment is also expected to file comments even if it only resubmits or incorporates by reference its former pleadings. It should also restate its present intention to apply for the channel if it is allotted and, if authorized, to build a station promptly. Failure to file may lead to denial of the request.

3. *Cut-off Procedures.* The following procedures will govern the consideration of filings in this proceeding.

(a) Counterproposals advanced in this proceeding itself will be considered if advanced in initial comments, so that parties may comment on them in reply comments. They will not be considered if advanced in reply comments. *(See* Section 1.420(d) of the Commission's Rules.)

(b) With respect to petitions for rule making which conflict with the proposal(s) in this *Notice,* they will be considered as comments in the proceeding, and Public Notice to this effect will be given as long as they are filed before the date for filing initial comments herein. If they are filed later than that, they will not be considered in connection with the decision in this docket.

(c) The filing of a counterproposal may lead the Commission to allot a different channel than was requested for any of the communities involved.

4. *Comments and Reply Comments; Service.* Pursuant to applicable procedures set out in Sections 1.415 and 1.420 of the Commission's Rules and Regulations, interested parties may file comments and reply comments on or before the dates set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached. All submissions by parties to this proceeding or by persons acting on behalf of such parties must be made in written comments, reply comments, or other appropriate pleadings. Comments shall be served on the petitioner by the person filing the comments. Reply comments shall be served on the person(s) who filed comments to which the reply is directed. Such comments and reply comments shall be accompanied by a certificate of service. *(See* Section 1.420(a), (b) and (c) of the Commission's Rules.) Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554.

5. *Number of Copies.* In accordance with the provisions of Section 1.420 of the Commission's Rules and Regulations, an original and four copies of all comments, reply comments, pleadings, briefs, or other documents shall be furnished the Commission.

6. *Public Inspection of Filings.* All filings made in this proceeding will be available for examination by interested parties during regular business hours in the Commission's Public Reference Room at its headquarters, 1919 M Street N.W., Washington, D.C.

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-38

In the Matter of

Amendment of Section 73.202(b), RM-8451
Table of Allotments,
FM Broadcast Stations.
(Sioux City, Iowa)

REPORT AND ORDER
(Proceeding Terminated)

Adopted: November 29, 1994; Released: December 8, 1994

By the Acting Chief, Allocations Branch:

1. At the request of Independent Communications, Inc. ("petitioner"), the Commission has before it the *Notice of Proposed Rule Making*, 9 FCC Rcd 2325 (1994), proposing the allotment of UHF Channel 39 to Sioux City, Iowa, as the community's fifth local television service. Petitioner filed comments restating its interest to apply for Channel 39, if allotted. Pappas Telecasting of the Midlands ("Pappas") filed comments and a counterproposal.[1]

2. Pappas suggested the allotment of Channel 44 instead of Channel 39 at Sioux City and submitted that due to spacing constraints imposed by the distance separation requirements of the Commission's Rules with respect to the antenna sites of other stations, the area within which a television broadcast station operating on Channel 39 for the purpose of providing service to Sioux City is limited. However, it notes that a transmitter site for Channel 44 can be used over a wide area, including the sites of all local television stations. Pappas states it will apply for Channel 44 if allotted to Sioux City, Iowa.

3. We believe the public interest would be served by allotting Channel 44 rather than Channel 39 to Sioux City, Iowa, as an additional television service. Our engineering staff has confirmed that use of the alternate channel opens a larger area available from which an applicant may choose a transmitter site. Channel 44 can be allotted to Sioux City with a positive offset[2] consistent with the minimum distance separation requirements of Sections 73.610 and 73.698 of the Commission's Rules without the imposition of a site restriction.[3] Furthermore this action is not affected by the TV freeze imposed in certain metropolitan areas.[4]

4. Accordingly, pursuant to the authority contained in Sections 4(i), 5(c)(1), 303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61, 0.204(b) and 0.283 of the Commission's Rules, IT IS ORDERED, That effective **January 23, 1995**, the TV Table of Allotments, Section 73.606(b) of the Commission's Rules, IS AMENDED, with respect to the community listed below, to read as follows:

City	Channel No.
Sioux City, Iowa	4-, 9, 14, *27-, 44+

5. IT IS FURTHER ORDERED, That this proceeding IS TERMINATED.

6. For further information concerning this proceeding, contact Pam Blumenthal, Mass Media Bureau, (202) 634-6530.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

[1] Although Pappas filed a pleading styled as a counterproposal, we do not considered Pappas's alternate channel suggestion to be a counterproposal since it does not introduce a new community or propose a higher class allotment than proposed in the *Notice*. *See Clinton, Saint Pauls and Southern Pines, North Carolina and Chesterfield, South Carolina*, 6 FCC Rcd 4370 (1991).

[2] A station with a "plus" or "minus" offset is required to operate with its carrier frequency 10 kHz above or below the normal carrier

[3] The coordinates for Channel 44 at Sioux City are North Latitude 42-29-30 and West Longitude 96-23-30.

[4] *See Order, Advance Television Systems and Their Impact on the Existing Television Broadcast Service*, 52 Fed. Reg. 28346, published July 29, 1987.

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-140

In the Matter of

Amendment of Section 73.202(b) RM-8543
Table of Allotments,
FM Broadcast Stations.
(Rapid City, South Dakota)

NOTICE OF PROPOSED RULE MAKING

Adopted: November 30, 1994; Released: December 8, 1994

Comment Date: January 30, 1995
Reply Comment Date: February 14, 1995

By the Acting Chief, Allocations Branch:

1. The Commission has before it the petition for rule making filed by Conway Broadcasting ("petitioner"), proposing the allotment of Channel 292C at Rapid City, South Dakota, as the community's sixth local FM transmission service. Petitioner states its intention to apply for the channel, if allotted.

2. We believe the proposal warrants consideration since it could provide the community with its sixth local FM transmission service. An engineering analysis has determined that Channel 292C can be allotted to Rapid City in compliance with the Commission's minimum distance separation requirements at city reference coordinates without the imposition of a site restriction.[1]

3. Accordingly, we will seek comments on the proposed amendment of the FM Table of Allotments, Section 73.202(b) of the Commission's Rules, for the community listed below, to read as follows:

	Channel No.	
City	Present	Proposed
Rapid City,	230C1, 250C1,	230C1, 250C1,
South Dakota	254C1, 262C1	254C1, 262C1
	281C1	281C1, 292C

4. The Commission's authority to institute rule making proceedings, showings required, cut-off procedures, and filing requirements are contained in the attached Appendix and are incorporated by reference herein. In particular, we note that a showing of continuing interest is required by paragraph 2 of the Appendix before a channel will be allotted.

5. Interested parties may file comments on or before **January 30, 1995**, and reply comments on or before **February 14, 1995**, and are advised to read the Appendix for the proper procedures. Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554. Additionally, a copy of such comments should be served on the petitioner, or its counsel or consultant, as follows:

Lars Conway
Conway Broadcasting
4415 Fremont Ave., South
Minneapolis, Minnesota 55409
(Petitioner)

6. The Commission has determined that the relevant provisions of the Regulatory Flexibility Act of 1980 do not apply to rule making proceedings to amend the FM Table of Allotments, Section 73.202(b) of the Commission's Rules. *See Certification That Sections 603 and 604 of the Regulatory Flexibility Act Do Not Apply to Rule Making to Amend Sections 73.202(b), 73.504 and 73.606(b) of the Commission's Rules*, 46 FR 11549, February 9, 1981.

7. For further information concerning this proceeding, contact Sharon P. McDonald, Mass Media Bureau, (202) 634-6530. For purposes of this restricted notice and comment rule making proceeding, members of the public are advised that no *ex parte* presentations are permitted from the time the Commission adopts a Notice of Proposed Rule Making until the proceeding has been decided and such decision is no longer subject to reconsideration by the Commission or review by any court. An *ex parte* presentation is not prohibited if specifically requested by the Commission or staff for the clarification or adduction of evidence or resolution of issues in the proceeding. However, any new written information elicited from such a request or a summary of any new oral information shall be served by the person making the presentation upon the other parties to the proceeding unless the Commission specifically waives this service requirement. Any comment which has not been served on the petitioner constitutes an *ex parte* presentation and shall not be considered in the proceeding. Any reply comment which has not been served on the person(s) who filed the comment, to which the reply is directed, constitutes an *ex parte* presentation and shall not be considered in the proceeding.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

[1] The coordinates for Channel 292C at Rapid City are North Latitude 44-04-50 and West Longitude 103-13-50.

APPENDIX

1. Pursuant to authority found in Sections 4(i), 5(c)(1),303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61 0.204(b) and 0.283 of the Commission's Rules, IT IS PROPOSED TO AMEND the FM Table of Allotments, Section 73.202(b) of the Commission's Rules and Regulations, as set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached.

2. *Showings Required.* Comments are invited on the proposal(s) discussed in the *Notice of Proposed Rule Making* to which this Appendix is attached. Proponent(s) will be expected to answer whatever questions are presented in initial comments. The proponent of a proposed allotment is also expected to file comments even if it only resubmits or incorporates by reference its former pleadings. It should also restate its present intention to apply for the channel if it is allotted and, if authorized, to build a station promptly. Failure to file may lead to denial of the request.

3. *Cut-off Procedures.* The following procedures will govern the consideration of filings in this proceeding.

(a) Counterproposals advanced in this proceeding itself will be considered if advanced in initial comments, so that parties may comment on them in reply comments. They will not be considered if advanced in reply comments. *(See* Section 1.420(d) of the Commission's Rules.)

(b) With respect to petitions for rule making which conflict with the proposal(s) in this *Notice,* they will be considered as comments in the proceeding, and Public Notice to this effect will be given as long as they are filed before the date for filing initial comments herein. If they are filed later than that, they will not be considered in connection with the decision in this docket.

(c) The filing of a counterproposal may lead the Commission to allot a different channel than was requested for any of the communities involved.

4. *Comments and Reply Comments; Service.* Pursuant to applicable procedures set out in Sections 1.415 and 1.420 of the Commission's Rules and Regulations, interested parties may file comments and reply comments on or before the dates set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached. All submissions by parties to this proceeding or by persons acting on behalf of such parties must be made in written comments, reply comments, or other appropriate pleadings. Comments shall be served on the petitioner by the person filing the comments. Reply comments shall be served on the person(s) who filed comments to which the reply is directed. Such comments and reply comments shall be accompanied by a certificate of service. *(See* Section 1.420(a), (b) and (c) of the Commission's Rules.) Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554.

5. *Number of Copies.* In accordance with the provisions of Section 1.420 of the Commission's Rules and Regulations, an original and four copies of all comments, reply comments, pleadings, briefs, or other documents shall be furnished the Commission.

6. *Public Inspection of Filings.* All filings made in this proceeding will be available for examination by interested parties during regular business hours in the Commission's Public Reference Room at its headquarters, 1919 M Street N.W., Washington, D.C.

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-141

In the Matter of

Amendment of Section 73.202(b) RM-8544

Table of Allotments,
FM Broadcast Stations.
(Dell Rapids, South Dakota)

NOTICE OF PROPOSED RULE MAKING

Adopted: November 30, 1994; Released: December 8, 1994

Comment Date: January 30, 1995
Reply Comment Date: February 14, 1995

By the Acting Chief, Allocations Branch:

1. The Commission has before it the petition for rule making filed by Conway Broadcasting ("petitioner"), proposing the allotment of Channel 239C3 at Dell Rapids, South Dakota, as the community's first local aural transmission service. Petitioner states its intention to apply for the channel, if allotted.

2. In support of the proposal, petitioner states that Dell Rapids is an incorporated town with its own municipal services, post office, zip code and indicia which define a "community" for allotment purposes.

3. We believe the public interest would be served by proposing the allotment of Channel 239C3 at Dell Rapids, South Dakota, since it could provide the community with its first local aural transmission service. An engineering analysis has determined that Channel 239C3 can be allotted to Dell Rapids in compliance with the Commission's minimum distance separation requirements with a site restriction of 3.1 kilometers (1.9 miles) southwest.[1]

4. Accordingly, we will seek comments on the proposed amendment of the FM Table of Allotments, Section 73.202(b) of the Commission's Rules, for the community listed below, to read as follows:

	Channel No.	
City	Present	Proposed
Dell Rapids, South Dakota	--	239C3

5. The Commission's authority to institute rule making proceedings, showings required, cut-off procedures, and filing requirements are contained in the attached Appendix and are incorporated by reference herein. In particular, we note that a showing of continuing interest is required by paragraph 2 of the Appendix before a channel will be allotted.

6. Interested parties may file comments on or before **January 30, 1995**, and reply comments on or before **February 14, 1995**, and are advised to read the Appendix for the proper procedures. Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554. Additionally, a copy of such comments should be served on the petitioner, or its counsel or consultant, as follows:

Lars Conway
Conway Broadcasting
4415 Fremont Ave., South
Minneapolis, Minnesota 55409
(Petitioner)

7. The Commission has determined that the relevant provisions of the Regulatory Flexibility Act of 1980 do not apply to rule making proceedings to amend the FM Table of Allotments, Section 73.202(b) of the Commission's Rules. *See Certification That Sections 603 and 604 of the Regulatory Flexibility Act Do Not Apply to Rule Making to Amend Sections 73.202(b), 73.504 and 73.606(b) of the Commission's Rules*, 46 FR 11549, February 9, 1981.

8. For further information concerning this proceeding, contact Sharon P. McDonald, Mass Media Bureau, (202) 634-6530. For purposes of this restricted notice and comment rule making proceeding, members of the public are advised that no *ex parte* presentations are permitted from the time the Commission adopts a Notice of Proposed Rule Making until the proceeding has been decided and such decision is no longer subject to reconsideration by the Commission or review by any court. An *ex parte* presentation is not prohibited if specifically requested by the Commission or staff for the clarification or adduction of evidence or resolution of issues in the proceeding. However, any new written information elicited from such a request or a summary of any new oral information shall be served by the person making the presentation upon the other parties to the proceeding unless the Commission specifically waives this service requirement. Any comment which has not been served on the petitioner constitutes an *ex parte* presentation and shall not be considered in the proceeding. Any reply comment which has not been served on the person(s) who filed the comment, to which the reply is directed, constitutes an *ex parte* presentation and shall not be considered in the proceeding.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

[1] The coordinates for Channel 239C3 at Dell Rapids are North Latitude 43-47-57 and West Longitude 96-43-01.

APPENDIX

1. Pursuant to authority found in Sections 4(i), 5(c)(1),303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61 0.204(b) and 0.283 of the Commission's Rules, IT IS PROPOSED TO AMEND the FM Table of Allotments, Section 73.202(b) of the Commission's Rules and Regulations, as set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached.

2. *Showings Required.* Comments are invited on the proposal(s) discussed in the *Notice of Proposed Rule Making* to which this Appendix is attached. Proponent(s) will be expected to answer whatever questions are presented in initial comments. The proponent of a proposed allotment is also expected to file comments even if it only resubmits or incorporates by reference its former pleadings. It should also restate its present intention to apply for the channel if it is allotted and, if authorized, to build a station promptly. Failure to file may lead to denial of the request.

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(a) Counterproposals advanced in this proceeding itself will be considered if advanced in initial comments, so that parties may comment on them in reply comments. They will not be considered if advanced in reply comments. *(See* Section 1.420(d) of the Commission's Rules.)

(b) With respect to petitions for rule making which conflict with the proposal(s) in this *Notice,* they will be considered as comments in the proceeding, and Public Notice to this effect will be given as long as they are filed before the date for filing initial comments herein. If they are filed later than that, they will not be considered in connection with the decision in this docket.

(c) The filing of a counterproposal may lead the Commission to allot a different channel than was requested for any of the communities involved.

4. *Comments and Reply Comments; Service.* Pursuant to applicable procedures set out in Sections 1.415 and 1.420 of the Commission's Rules and Regulations, interested parties may file comments and reply comments on or before the dates set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached. All submissions by parties to this proceeding or by persons acting on behalf of such parties must be made in written comments, reply comments, or other appropriate pleadings. Comments shall be served on the petitioner by the person filing the comments. Reply comments shall be served on the person(s) who filed comments to which the reply is directed. Such comments and reply comments shall be accompanied by a certificate of service. *(See* Section 1.420(a), (b) and (c) of the Commission's Rules.) Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554.

5. *Number of Copies.* In accordance with the provisions of Section 1.420 of the Commission's Rules and Regulations, an original and four copies of all comments, reply comments, pleadings, briefs, or other documents shall be furnished the Commission.

6. *Public Inspection of Filings.* All filings made in this proceeding will be available for examination by interested parties during regular business hours in the Commission's Public Reference Room at its headquarters, 1919 M Street N.W., Washington, D.C.

Before the
Federal Communications Commission
Washington, D.C. 20554

LETTER
November 30, 1994

IN REPLY REFER TO:
DA 94-1346

Mr. Frederick Kuperberg
Senior Vice President
Business and Legal Affairs
The Disney Channel
3800 West Alameda Avenue
Burbank, California 91505-6070

Dear Mr. Kuperberg:

This is in response to your letter of November 23, 1994, requesting expedited clarification of the Commission's notice requirements as applied to the scheduled addition of The Disney Channel to cable programming service tiers ("CPSTs") prior to January 1, 1995.

According to your letter, The Disney Channel has held discussions with numerous cable operators regarding the reconfiguration of The Disney Channel from an expensive per channel offering to a more affordable and widely distributed CPST service. In particular, The Disney Channel has been negotiating to add The Disney Channel to CPSTs "as soon as the Commission's 'going forward' rule revisions become effective."[1] Accordingly, one large unnamed multiple system operator ("MSO") discussed in your letter plans to move The Disney Channel to a regulated CPST on December 31, 1994, and to adjust its rates in accordance with the Commission's revised going forward regulations on January 1, 1995. You request expedited clarification of the Commission's notice requirements to allow the MSO to provide initial notice of these service and rate adjustments to subscribers using alternative means, including newspaper and on-screen announcements. According to your letter, this particular MSO uses cycle billing and it would be impossible for the MSO to comply literally with the Commission's subscriber notification rules because it is no longer possible to include such notification in a billing cycle which will be delivered to all customers at least 30 days prior to December 31, 1994. You state that, even if a separate mailing could be prepared, such a mailing would be unduly costly and burdensome.

Pursuant to Sections 76.964 and 76.309(c)(3)(i)(B) of the Commission's rules, cable operators are required to provide subscribers and local franchising authorities with thirty days written notice of any rate or service change. These rules are intended in part to provide subscribers ample time to react and, if they so elect, to cancel any service they no longer wish to receive due to the rate or service change. We believe, however, that, under the limited circumstances described in your letter, and given the transitional nature of your request, a waiver of our notice provisions is appropriate. We note that adding a channel to a CPST (or to a basic service tier where an operator offers only one tier of regulated cable service) on January 1, 1995, as provided in our *Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking* in MM Docket Nos. 92-266 and 93-216, FCC 94-286 (released November 18, 1994) (*"Sixth Reconsideration Order"*), and literal compliance with the referenced notice regulations, is not feasible given the time frame between the release of *Sixth Reconsideration Order* and the effective date of our revised going forward rules adopted therein. We also believe that the conditions to this waiver described below will adequately protect subscribers from undue harm.

We therefore waive our notice requirements contained in Sections 76.964 and 76.309(c)(3)(i)(B) of the Commission's rules with respect to the addition of The Disney Channel to CPSTs prior to January 1, 1995, with the corresponding rate increase effective on January 1, 1995. We limit this waiver, however, to the circumstances described in your November 23, 1994 letter, including but not limited to an operator's compliance with the substitute advance notice procedures described in your letter, namely newspaper advertisements in each affected cable community, on-screen messages on a daily basis, notifying local franchising authorities as soon as practicable, and written notice to subscribers beginning in mid to late December.[2] Because our notification rules are intended in part to provide subscribers with the opportunity to cancel any service they no longer wish to receive due to a rate or service change, we will require, as a further condition of this waiver, that, if any subscriber cancels his or her subscription to the relevant CPST within thirty days after the date of the first bill reflecting the increased rate, the operator must refund to that subscriber the incremental dollar amount attributable to the addition of The Disney Channel to the CPST from December 31, 1994 (the date The Disney Channel will be added to the CPSTs) to the date the subscriber cancels the CPST.

Sincerely,

Meredith J. Jones
Chief, Cable Services Bureau

[1] Letter from Frederick Kuperberg, Vice President, Business and Legal Affairs, The Disney Channel, to Meredith J. Jones, Chief, Cable Services Bureau, dated November 23, 1994, at 2.

[2] We note that we have previously granted waivers of our notice provisions in transitional situtations where the cable operator provides similar substitute advance notice. *See, e.g., In re fX* (released May 9, 1994) (providing limited waiver of notice provisions in 47 C.F.R. §§ 76.964 and 76.309(c)(3) as applied to the launch of the new fX channel).

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

STAR CABLE ASSOCIATES

Petition for Reconsideration

of the Certification of Hubbard Township, Ohio
to Regulate Basic Cable Rates
(OH1967)

MEMORANDUM OPINION AND ORDER

Adopted: November 30, 1994; Released: December 1, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On January 7, 1994, Star Cable Associates ("Star Cable") filed a timely petition for reconsideration challenging the certification of the Hubbard Township Board of Trustees to regulate rates for basic cable service and associated equipment in Hubbard, Ohio.[1] Hubbard Township did not file an opposition to Star Cable's petition.

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are "not subject to effective competition.[2] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[3] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[4] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[5] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[6]

II. DISCUSSION

3. Star Cable argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in the unincorporated areas of Hubbard Township, its franchise area.[7] Star Cable claims that it currently serves only 195 of the 2,388 households (that is, occupied housing units)[8] in its franchise area, or 8 percent of the total number of households. As supporting documentation, Star Cable provides 1990 Census data[9] which shows that there are 2,388 households in the unincorporated areas of Hubbard Township. Star Cable also submits a computer print-out with sufficient subscriber information to support its claim that it serves 195 households in the franchise area. Finally, Star Cable provides an affidavit by a responsible official certifying the accuracy of the data included in the petition.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[10] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[11] Star Cable has met this burden. Star Cable appropriately relied on data reflecting the number of households as required by our rules.[12] Relying on this data, Star Cable has submitted sufficient evidence demonstrating that its cable system serving Hubbard Township, its franchise area, serves 195 of the 2,388 households, or 8 percent of the households, within its franchise area. Thus, we find Star Cable's system serving Hubbard Township is subject to effective competition. Accordingly, its petition is granted.

---

[1] Hubbard Township filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on November 15, 1993, which became effective on December 15, 1993.

[2] 47 U.S.C. § 543(a)(4).

[3] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[4] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition.47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[5] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[6] 47 C.F.R. § 76.911(c).

[7] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[8] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*"Third Recon. Order"*). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[9] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994).

[10] 47 C.F.R. § 76.906.

[11] 47 C.F.R. § 76.911(b)(1).

[12] *Third Recon. Order, supra.*

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Star Cable challenging the certification of the Hubbard Township Board of Trustees to regulate basic cable rates IS GRANTED.

6. IT IS FURTHER ORDERED that the certification of the Hubbard Township Board of Trustees to regulate Star Cable's basic cable rates IS RESCINDED.

7. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

STAR CABLE ASSOCIATES

Petition for Reconsideration

of the Certification of
Kinsman Township, Ohio
to Regulate Basic Cable Rates
(OH2072)

MEMORANDUM OPINION AND ORDER

Adopted: November 30, 1994; Released: December 1, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On December 20, 1993, Star Cable Associates ("Star Cable") filed a timely petition for reconsideration challenging the certification of Kinsman Township, Ohio to regulate rates for basic cable service and associated equipment.[1] Kinsman Township did not file an opposition to Star Cable's petition.

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[2] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[3] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[4] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[5] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[6]

II. DISCUSSION

3. Star Cable argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in Kinsman Township, its franchise area.[7] Star Cable claims that it currently serves only 53 of the 742 households (that is, occupied housing units)[8] in its franchise area, or 7 percent of the total number of households. As supporting documentation, Star Cable provides 1990 Census data[9] which shows that there are 742 households in Kinsman Township. Star Cable also submits a computer print-out with sufficient subscriber information to support its claim that it serves 53 households in the franchise area. Finally, Star Cable provides an affidavit by a responsible official certifying the accuracy of the data included in the petition.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[10] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[11] Star Cable has met this burden. Star Cable appropriately relied on data reflecting the number of households as required by our rules.[12] Relying on this data, Star Cable has submitted sufficient evidence demonstrating that its cable system serving Kinsman Township, its franchise area, serves 53 of the 742 households, or 7 percent of the households, within its franchise area. Thus, we find Star Cable's system serving Kinsman Township is subject to effective competition. Accordingly, its petition is granted.

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[1] Kinsman Township filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on October 21, 1993, which became effective on November 20, 1993.

[2] 47 U.S.C. § 543(a)(4).

[3] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[4] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition.47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[5] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[6] 47 C.F.R. § 76.911(c).

[7] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[8] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*"Third Recon. Order"*). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[9] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994).

[10] 47 C.F.R. § 76.906.

[11] 47 C.F.R. § 76.911(b)(1).

[12] *Third Recon. Order, supra.*

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Star Cable challenging the certification of Kinsman Township to regulate basic cable rates IS GRANTED.

6. IT IS FURTHER ORDERED that the certification of Kinsman Township to regulate Star Cable's basic cable rates IS RESCINDED.

7. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

CABLEVISION, CABLE
MANAGEMENT ASSOCIATES

Petition for Reconsideration

of the Certification of
Ouachita Parish Police Jury, Louisiana,
to Regulate Basic Cable Service Rates
(LA0163, LA0164, LA0321)

MEMORANDUM OPINION AND ORDER

Adopted: November 30, 1994; Released: December 1, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On October 29, 1993, Cablevision, Cable Management Services ("CMA") submitted a timely-filed petition for reconsideration[1] challenging the certification of Ouachita Parish Police Jury ("Ouachita") to regulate the system's rates for basic cable service rates and associated equipment in South Monroe, LA (LA0163), North Monroe, LA (LA0164), and Calhoun, LA (LA0321).[2] Ouachita did not file an opposition to CMA's petition.

2. Section 623(a)(4) of the Communications Act, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[3] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition unless the franchising authority has actual knowledge to the contrary.[4] Certification becomes effective 30 days from the date of filing unless the Commission finds that the authority does not meet the statutory certification requirements.[5] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days of the effective date of such certification.[6] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[7]

II. DISCUSSION

3. In its petition, CMA alleges that its rates are exempt from regulation because its system serves fewer that 30 per cent of the households in the franchise area.[8] CMA claims that it serves only 2,434 of the 50,000 "houses" in the parish. No other information or supporting documentation is provided.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[9] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within its franchise area.[10] CMA has not met this burden. First, CMA did not submit any supporting documentation to support its claim. Second, based on the information before us, it appears that CMA's claim is inappropriately based on the number of houses in the franchising area. Our rules, however, require the use of data reflecting the number of "households" (*i.e.*, occupied housing units) in the franchise area. *Third Order on Reconsideration*, in MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994).[11]

5. Third, CMA has apparently aggregated the number of subscribers and "houses" for more than one cable system. CMA claims that its "cable *systems* should not be regulated since fewer than 30 per cent of the households subscribe to our service." (emphasis added). This language indicates that

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[1] CMA's challenge, although clearly in opposition to Ouachita's certification, does not state that it is a petition for reconsideration. We note, however, that this challenge was filed within 30 days of the date certification became effective as required by our rules, 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd, 5631, 5693 (1993) (*"Rate Order"*). Thus, we find that consideration of this challenge as a petition for reconsideration serves the public interest.

[2] Ouachita filed its Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Effective Competition ("FCC Form 328") on September 17, 1993. Its certification became effective on October 17, 1993.

[3] 47 U.S.C. § 543(a)(4).

[4] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[5] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: (1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; (2) the franchising authority lacks the legal authority to adopt, and the personnel to administer, rate regulations; (3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or (4) the cable system in question is subject to effective competition. 47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[6] 47 C.F.R. §§ 1.106, 76.911; *Rate Order*, at 5693.

[7] 47 C.F.R. § 76.911(c).

[8] The Commission's rules provide that only the rates of cable systems that are subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the cable service of a cable system. 47 C.F.R. § 76.905(a) and (b)(1).

[9] 47 C.F.R. § 76.906.

[10] 47 C.F.R. § 76.911(b)(1).

[11] As the Commission stated in the *Third Recon. Order*, "[a]s used in the Cable Act, we presume that Congress did not intend "households" to have a different meaning than in the 1990 Census that would include vacant units or even partial year vacant units. "*Third Recon. Order, supra*. The term "household" is defined for purposes of the 1990 Census Data as "all the persons who occupy a housing unit." Bureau of Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8. Thus, the term reflects only occupied housing units.

CMA is referring to more than one cable system; however, it does not disclose the exact number. As the Commission previously stated, effective competition must be demonstrated for each cable system, regardless of whether the systems in question are all located within one franchise area.[12]

6. Finally, CMA has not demonstrated that its effective competition claim is made on a franchise area basis. Specifically, CMA alleges effective competition with respect to three communities. However, there are no facts from which we can determine whether these communities represent separate franchise areas. If they do, a separate effective competition showing must be made for each separate franchise area where certification is challenged since the rules in question are administered on a franchise-area by franchise-area basis.[13] As CMA did not measure its penetration level in a manner that is consistent with the Commission's rules and policies, it has failed to demonstrate that effective competition exists. Accordingly, we deny its petition.

III. ORDERING CLAUSES

7. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Cablevision, Cable Management Associates, Inc. challenging the certification of Ouachita Parish Police Jury, LA to regulate Blue Ridge's basic cable rates IS DENIED.

8. IT IS FURTHER ORDERED that the automatic stay imposed by Section 76.911(c) of the Commission's Rules, as amended, 47 C.F.R. § 76.911(c) IS TERMINATED.

9. IT IS FURTHER ORDERED that Cablevision, Cable Management Associates Inc. SHALL FILE the required rate justifications on the appropriate forms with Ouachita Parish Police Jury, LA within 30 days of the release date of this *Memorandum Opinion and Order* or within 30 days of receipt of notice from Ouachita Parish Police Jury, LA that it is regulating rates, whichever is later.

10. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's Rules, as amended, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[12] *Rate Order*, at 5672.
[13] *Rate Order*, at 5672.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

LARIBAY CABLEVISION

Petition for Reconsideration

of the Certification of
Concordia Parish Police Jury, Louisiana,
to Regulate Basic Cable Service Rates
(LA0178)

MEMORANDUM OPINION AND ORDER

Adopted: November 30, 1994; Released: December 1, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On October 25, 1993, Laribay Cablevision ("Laribay") submitted a timely-filed petition for reconsideration[1] challenging the certification of Concordia Parish Police Jury ("Concordia") to regulate the system's rates for basic cable service and associated equipment.[2] Concordia did not file anopposition.

2. Section 623(a)(4) of the Communications Act, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[3] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition unless the franchising authority has actual knowledge to the contrary.[4] Certification becomes effective 30 days from the date of filing unless the Commission finds that the authority does not meet the statutory certification requirements.[5] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days of the effective date of such certification.[6] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[7]

II. DISCUSSION

3. In its petition, Laribay alleges that its rates are exempt from regulation because its system "has fewer than 30 per cent of the households in the franchise area that subscribe to the cable service of its cable system."[8] Laribay presents no specific facts or documentation to support this conclusory allegation.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[9] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within its franchise area.[10] Based on the evidence, we find that Laribay has not met this burden. Specifically, Laribay does not indicate the number of households within its franchise area or the number of households which subscribe to its cable service. In addition, it does not provide any documentation to support its claim. Accordingly, it has failed to demonstrate that effective competition exists and, therefore, we deny its petition.

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Laribay Cablevision challenging the certification of Concordia Parish Police Jury to regulate Laribay's basic cable rates IS DENIED.

6. IT IS FURTHER ORDERED that the automatic stay imposed by Section 76.911(c) of the Commission's Rules, as amended, 47 C.F.R. § 76.911(c) IS TERMINATED.

7. IT IS FURTHER ORDERED that Laribay Cablevision SHALL FILE the required rate justifications on the appropriate forms with Concordia Parish Police Jury within 30 days of the release date of this *Memorandum Opinion and Order* or within 30 days of receipt of notice from Concordia Parish Police Jury that it is regulating rates, whichever is later.

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[1] Laribay's challenge, although clearly in opposition to Concordia's certification, does not state that it is a petition for reconsideration. We note, however, that this challenge was filed within 30 days of the date certification became effective as required by our rules, 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd, 5631, 5693 (1993) (*"Rate Order"*). Thus, we find that consideration of this challenge as a petition for reconsideration serves the public interest.

[2] Concordia filed its Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Effective Competition ("FCC Form 328") on October 20, 1993. Its certification became effective on November 19, 1993.

[3] 47 U.S.C. § 543(a)(4).

[4] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[5] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: (1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; (2) the franchising authority lacks the legal authority to adopt, and the personnel to administer, rate regulations; (3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or (4) the cable system in question is subject to effective competition. 47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[6] 47 C.F.R. §§ 1.106, 76.911; *Rate Order*, at 5693.

[7] 47 C.F.R. § 76.911(c).

[8] The Commission's rules provide that only the rates of cable systems that are subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the cable service of a cable system. 47 C.F.R. §76.905(a) and (b)(1).

[9] 47 C.F.R. § 76.906.

[10] 47 C.F.R. § 76.911(b)(1).

8. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's Rules, as amended, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

LARIBAY CABLEVISION

Petition for Reconsideration

of the Certification of
Catahoula Parish Police Jury, Louisiana,
to Regulate Basic Cable Service Rates
(LA0390)

MEMORANDUM OPINION AND ORDER

Adopted: November 30, 1994; Released: December 1, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On October 13, 1993, Laribay Cablevision ("Laribay") submitted a timely-filed petition for reconsideration[1] challenging the certification of Catahoula Parish Police Jury ("Catahoula") to regulate the system's rates for basic cable service and associated equipment.[2] Catahoula did not file an opposition.

2. Section 623(a)(4) of the Communications Act, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[3] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition unless the franchising authority has actual knowledge to the contrary.[4] Certification becomes effective 30 days from the date of filing unless the Commission finds that the authority does not meet the statutory certification requirements.[5] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days of the effective date of such certification.[6] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[7]

II. DISCUSSION

3. Laribay alleges that its rates are exempt from regulation because its system has fewer than 30 per cent of the households in the franchise area that subscribe to the cable service of its cable system.[8] Laribay presents no specific facts or documentation to support this conclusory allegation.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[9] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within its franchise area.[10] Based on the evidence, we find that Laribay has not met this burden. Specifically, Laribay does not indicate the number of households within its franchise area or the number of households which subscribe to its cable service. In addition, it does not provide any documentation to support its claim. Accordingly, it has failed to demonstrate that effective competition exists and, therefore, we deny its petition.

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Laribay Cablevision challenging the certification of Catahoula Parish Police Jury to regulate Laribay's basic cable rates IS DENIED.

6. IT IS FURTHER ORDERED that the automatic stay imposed by Section 76.911(c) of the Commission's Rules, as amended, 47 C.F.R. § 76.911(c) IS TERMINATED.

7. IT IS FURTHER ORDERED that Laribay Cablevision SHALL FILE the required rate justifications on the appropriate forms with Catahoula Parish Police Jury within 30 days of the release date of this *Memorandum Opinion and Order* or within 30 days of receipt of notice from Catahoula Parish Police Jury that it is regulating rates, whichever is later.

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[1] Laribay's challenge, although clearly in opposition to Catahoula's certification, does not state that it is a petition for reconsideration. We note, however, that this challenge was filed within 30 days of the date certification became effective as required by our rules, 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd, 5631, 5693 (1993) (*"Rate Order"*). Thus, we find that consideration of this challenge as a petition for reconsideration serves the public interest.

[2] Catahoula filed its Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Effective Competition ("FCC Form 328") on October 7, 1993. Its certification became effective on November 6, 1993.

[3] 47 U.S.C. § 543(a)(4).

[4] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[5] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: (1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; (2) the franchising authority lacks the legal authority to adopt, and the personnel to administer, rate regulations; (3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or (4) the cable system in question is subject to effective competition. 47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[6] 47 C.F.R. §§ 1.106, 76.911; *Rate Order*, at 5693.

[7] 47 C.F.R. § 76.911(c).

[8] The Commission's rules provide that only the rates of cable systems that are subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the cable service of a cable system. 47 C.F.R. § 76.905(a) and (b)(1).

[9] 47 C.F.R. § 76.906.

[10] 47 C.F.R. § 76.911(b)(1).

8. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's Rules, as amended, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

HORIZON CABLE I
LIMITED PARTNERSHIP

Petition for Reconsideration

of Certification of
Green Oak Township (MI0905)
To Regulate Basic Cable Rates

MEMORANDUM OPINION AND ORDER

Adopted: December 1, 1994; Released: December 1, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On November 12, 1993, Horizon Cable I Limited Partnership ("Horizon"), filed a timely petition for reconsideration challenging the certification of Green Oak Township ("Green Oak") to regulate the system's rates for basic cable service and associated equipment.[1] Green Oak filed an objection to Horizon's petition for reconsideration to which Horizon filed a reply. In addition, both parties filed additional pleadings pursuant to the Commission's July 29, 1994 Order.[2]

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators which are not subject to effective competition.[3] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless the franchising authority has actual knowledge to the contrary.[4] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[5] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[6] Regulation of rates is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[7]

II. DISCUSSION

Horizon's Effective Competition Claim

3. Horizon argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in Green Oak Township, its franchise area.[8] Horizon claims that it serves only 538 of the 4,256 "homes" in its franchise area, or 13 percent of the total number of "homes." As supporting documentation, Horizon provides a copy of the relevant page of the 1990 Census data which shows that there are 4,256 "housing units" in Green Oak Township. In addition, Horizon submits a copy of a subscriber printout dated October 21, 1993, which demonstrates that Horizon has 538 subscribers. Finally, Horizon provides a declaration under penalty of perjury by a responsible official certifying to the accuracy of the data included in the petition.[9]

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[10] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's rules, is present within the franchise area.[11] Horizon has failed to meet this burden. Specifically, Horizon inappropriately relied upon "housing unit" data rather than "household" data to support its effective competition claim. Horizon's claim is inappropriately based on the number of housing units (that is, occupied and vacant units) within the franchise area. Our rules, however, require the use of data reflecting the number of "households" (*i.e.*, occupied housing units) in the franchise area. *See Third Order on Reconsideration*, in MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*"Third Recon. Order"*).[12] As Horizon has failed to base its effective competition claim on household data as required by our rules, we will deny its petition.

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[1] Green Oak Township filed a Certification of Franchising Authority to Regulate Basic Cable Rates and Initial Finding of Lack of Effective Competition (FCC Form 328) with the Commission on October 1, 1993. Certification became effective on October 31, 1993.

[2] *Cable Operators' Petitions for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994) (*"Effective Competition Order"*).

[3] 47 U.S.C. § 543(a)(4).

[4] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[5] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: (1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; (2) the franchising authority lacks the legal authority to adopt, and the personnel to administer, rate regulations; (3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or (4) the cable system in question is subject to effective competition.47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[6] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, in MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[7] 47 C.F.R. § 76.911(c).

[8] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's cable service. 47 C.F.R. § 76.905(a) and (b)(1).

[9] Declaration of Alan Baird, General Manager, dated November 10, 1993.

[10] 47 C.F.R. § 76.906.

[11] 47 C.F.R. § 76.911(b).

[12] As the Commission stated in the *Third Recon. Order*, "[a]s

Other Matters

5. In its objection to Horizon's petition, Green Oak argues that Horizon is not subject to effective competition because it has "redefined" its franchise area. Green Oak alleges that Horizon has made an affirmative decision to limit its service area to scattered areas in the southeastern portion of Green Oak even though its franchise does not restrict service to a specific area of the township. In light of this, Green Oak argues that Horizon's showing of effective competition must be based on its "redefined" franchise area. In reply, Horizon denies Green Oak's allegation, asserting that the terms of its franchise agreement with Green Oak require Horizon to expand into unserved areas of the township when population density reaches a level of 30 households per cable mile. Horizon claims that it has been expanding its service area in Green Oak on an on-going basis, and has increased the number of homes passed in Green Oak by 37 percent over the past three years. In light of our decision that Horizon has failed to rely on appropriate housing data for purposes of demonstrating effective competition, we see no need to address Green Oak's argument at this time.

III. ORDERING CLAUSES

6. Accordingly, IT IS ORDERED that the petition for reconsideration filed by Horizon Cable I Limited Partnership challenging the certification of Green Oak Township to regulate Horizon's basic cable service rates IS DENIED.

7. IT IS FURTHER ORDERED that the automatic stay imposed by Section 76.911(c) of the Commission's Rules, as amended, 47 C.F.R. § 76.911(c) IS TERMINATED.

8. IT IS FURTHER ORDERED that Horizon SHALL FILE the required rate justifications on the appropriate forms with Green Oak Township, MI within thirty (30) days of the release date of this *Memorandum Opinion and Order* or within thirty (30) days of receipt of notice from the franchising authority that it is regulating Horizon's rates, whichever is later.

9. This action is taken pursuant to delegated authority under Section 0.321 of the Commission's rules, as amended, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

used in the Cable Act, we presume that Congress did not intend "households" to have a different meaning than in the 1990 Census that would include vacant units or even partial year vacant units." *Third Recon. Order, supra.* The term "household" is defined for purposes of the 1990 Census data as "all the persons who occupy a housing unit." Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8. Thus, the term reflects only occupied housing units. The term "housing unit," however, was defined by the Census Bureau to include both occupied and vacant housing units.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Dimension Cable Services, LOI-93-37
Rancho Palos Verdes, California

Letter of Inquiry

MEMORANDUM OPINION AND ORDER

Adopted: November 23, 1994; Released: November 25, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. A subscriber of Times Mirror Cable Television of Palos Verdes Peninsula, Inc., d/b/a Dimension Cable Services ("Dimension Cable"), filed an FCC Form 329 complaint dated October 15, 1993, that alleged violations by Dimension Cable of Commission regulations governing cable television. In response to this complaint, the Commission issued Letter of Inquiry 93-37 ("LOI") to Dimension Cable on December 13, 1993.[1] The LOI asked Dimension Cable to provide information concerning its compliance with the Commission's rules governing evasion in the offering of packages which allegedly are not rate-regulated. Dimension Cable responded to our LOI on January 13, 1994.

II. BACKGROUND

2. In the Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act"), Congress created a regulatory scheme giving the Commission and local franchising authorities jurisdiction over the cable programming and equipment rates of non-competitive cable systems. The 1992 Cable Act provides that the rates of cable systems not subject to effective competition may be regulated by local franchising authorities, in the case of basic service, and by the Commission, in the case of cable programming services.[2] A stated policy of the 1992 Cable Act is to ensure that "consumer interests are protected in the receipt of cable service."[3]

3. The 1992 Cable Act requires cable operators to offer subscribers a basic tier that must contain at least all qualified local broadcast signals and, unless otherwise specified by the local franchising authority, public, educational, and governmental channels.[4] The Commission was charged by the 1992 Cable Act with creating regulations that ensure that the rates for the basic service tier are reasonable.[5] The 1992 Cable Act directs that "[s]uch regulations shall be designed to achieve the goal of protecting subscribers of any cable system that is not subject to effective competition from rates for the basic service tier that exceed the rates that would be charged for the basic service tier if such cable system were subject to effective competition."[6] Under the 1992 Cable Act, operators may offer other channels in a cable programming service tier or tiers.[7] The 1992 Cable Act orders the Commission to create regulations for the cable programming service tiers that allow it to identify individual cases of unreasonable rates.[8] The 1992 Cable Act thus protects consumers' interests in continuing to receive the basic service tier and cable programming service tiers at reasonable rates.

4. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[9] The 1992 Cable Act's legislative history states that the Commission should scrutinize offerings of non-traditional stand-alone services to "prevent repricing, retiering, or other alterations of rate structures" that could have the effect of evading the purposes of rate regulation.[10] This provision in the 1992 Cable Act is intended to give the Commission the authority to address changes in the cable industry's business practices that would thwart the intent of rate regulation.[11]

5. In the *Rate Order* the Commission defined evasion as "any practice or action which avoids the rate regulation provisions of the Cable Act or Commission rules contrary to the intent of the Act or its underlying policies."[12] We must scrutinize a particular operator's marketing or pricing

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[1] Letter from Roy J. Stewart, Chief, Mass Media Bureau, FCC, to Dimension Cable Services, LOI-93-37 (December 13, 1993). Copies of the Letter of Inquiry and Response are available to the public in the FCC's Cable Reference Center, 2033 M Street, N.W., Room 207, Washington, D.C. We also note that there is a pending rate complaint proceeding involving Dimension Cable. Our decision made herein will be made a part of that proceeding. Thus, for example, we will not order Dimension Cable to make refunds to subscribers in regard to Dimension Cable's purported "a la carte" restructuring. Obviously, however, we may order refunds if we find violations of other rules that should result in refunds.

[2] Communications Act of 1934 § 623 (a)(2), 47 U.S.C. § 543 (a)(2)(1992).

[3] Pub. L. No. 102-385 § 2 (b) (4) (1992); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. at 34 (1992).

[4] Communications Act of 1934 § 623 (b)(7)(A)(ii-iii), 47 U.S.C. § 543 (b)(7)(A)(ii-iii)(1992); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket 92-266, *Report and Order and Further Notice of Proposed Rulemaking,* 8 FCC Rcd 5631 ¶ 157-161 (1993) (*"Rate Order"*) (franchising authorities may require operators to carry PEG channels on tiers other than basic).

[5] Communications Act of 1934 § 623 (b)(1), 47 U.S.C. § 543 (b)(1)(1992).

[6] *Id.*

[7] Communications Act of 1934 § 623(l)(2), 47 U.S.C. § 543(l)(2)(1992).

[8] Communications Act of 1934 § 623 (c)(1)(A), 47 U.S.C. § 543 (c)(1)(A)(1992). Identification of individual cases of unreasonable rates is achieved by a process in which the Commission assumes jurisdiction over systems where a complaint about a cable programming service tier rate is filed.

[9] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[10] H.R. Rep. No. 628, 102d Cong., 2d Sess. at 79 (1992).

[11] S. Rep. No. 92, 102d Cong., 2d Sess. at 77 (1992).

[12] *Rate Order* ¶ 451.

practices to determine whether those practices have the effect of avoiding the requirements of our rate regulations, contrary to the intent of the 1992 Cable Act and our rules.

III. FACTS

6. Before the effective date of the Commission's rate rules, Dimension Cable's services included: a 22 channel basic tier for $12.95; an 11 channel cable programming service tier call Dimension for $5.50; a 10 channel cable programming service tier called Preferred Dimension for $3.00; and five premium channels offered on a per-channel or package basis. Only customers whose television sets were not capable of receiving all 43 channels needed converters to receive these services. Customers needed addressable converters to subscribe to the five premium channels.

7. The following chart summarizes Dimension Cable's service tier offerings prior to September 1, 1993:

Offering	Channels	Price
1. Basic	22	$12.95
2. Dimension	11	$5.50
3. Preferred Dimension	10	$3.00
Total	43	$21.45

8. On August 31, 1993, the day before cable rate regulation became effective, Dimension Cable restructured its programming services to add a la carte offerings. It states that it moved four channels, American Movie Classics, Turner Network Television, The Nashville Network and The Discovery Channel, from the Preferred Dimension tier and offered them a la carte at a price of $.75 each. The four a la carte channels were also sold in a package for $1.50. Dimension Cable's restructuring also included the consolidating of its two cable programming services tiers into one cable programming service tier with a total of 17 channels. Its basic tier cost $13.65 and its new Dimension cable programming service tier cost $8.40. Only customers who needed converters before the restructuring needed them to receive the a la carte channels. Although waived for the first 30 days, Dimension Cable charges customers for switching among these services.

9. The following chart summarizes Dimension Cable's service tier options as of the date of its response to our LOI:[13]

Offering	Channels	Price
1. Basic	22	$13.65
2. Dimension	17	$8.40
3. Package	4	$1.50
Total	43	$23.55

10. Dimension Cable states that existing customers bought the package at a rate of 98.5 percent. As of January 13, 1994, 23 of Dimension Cable's customers chose to receive one or more individual a la carte channels while 11,718 subscribed to the package.

IV. DISCUSSION

11. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering.[14] An evasion, as defined by the Commission, is an act or practice that "avoids the rate regulation provisions of the [Cable] Act or our rules contrary to the intent of the Act or its underlying policies."[15] In the *Rate Order*, we stated that "retiering otherwise permitted under our rules will not be deemed an evasion."[16] First, we examine whether Dimension Cable's response to the LOI shows that its restructuring of its offerings had the effect of evading rate regulation for the channels that Congress intended to be rate-regulated.

12. Dimension Cable's restructuring effective September 1, 1993, involved its movement of four channels (American Movie Classics, Turner Network Television, The Nashville Network and The Discovery Channel) from its 10 channel Preferred Dimension tier to create the four-channel package that it alleges is not rate-regulated. Thus, Dimension Cable removed channels from otherwise rate-regulated tiers to create a new package of channels. In so doing, Dimension Cable avoided application of our rate regulations which generally required cable operators to reduce rates by about 10 percent. That is, if Dimension Cable had not restructured on September 1, 1993, it would have been required to recalculate its rates in accordance with the *Rate Order* we released on May 3, 1993, which generally required cable operators to reduce their rates. Moreover, customers that were receiving the four cable programming service tier channels at issue continued to receive them after the restructuring, and there appears to be no sufficient justification for Dimension Cable's restructuring other than to avoid rate regulation.

13. Other factors corroborate our view that Dimension Cable's restructuring may have had the effect of avoiding rate regulation. First, it offered this package on the eve of regulation. Second, it automatically subscribed its customers to the offerings that previously had been part of its cable programming service tiers. In light of these facts, it appears that Dimension Cable's restructuring of its offerings may have evaded rate regulation. We will not find an actual evasion occurred, however, if Dimension Cable's action complied with our a la carte policy that was in effect at the time of its restructuring. If the offering met our requirements for a permissible collective offering of a la carte channels, then Dimension Cable would not have evaded our rate regulations because it would not be required to reduce its price for the collective a la carte package.[17]

14. In our *Rate Order*, the Commission recognized that "a la carte packages" appear to be "cable programming services," but said that "interpreting the statute in such a literal fashion could disadvantage consumers by denying them discounts on packages of per-channel or per-program services and by limiting subscriber access to a greater quan-

[13] This Order does not evaluate Dimension Cable's rates for its basic and cable programming service tiers. These rates are subject to review by the local franchising authority and the Commission in separate proceedings.

[14] Communications Act of 1934 § 623(h), 47 U.S.C. § 8543(h)(1992).

[15] *Rate Order* ¶ 451.

[16] *Id.* at ¶ 453.

[17] In our *Going Forward Order*, we have reconsidered our regulatory treatment of collective offerings of a la carte channels. *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Sixth Order on*

tity of premium programming."[18] Thus, we envisioned that cable operators, for the most part, would offer channels that previously had been offered a la carte in discounted packages, and concluded that it would be better for consumers if we construed the 1992 Cable Act to permit such discounting.[19] This is not the type of offering that Dimension Cable and others have provided their subscribers. Specifically, these operators did not offer a discounted package of channels that previously had been offered a la carte to subscribers, but instead removed channels from a tier that would be subject to our rate regulations.

15. Moreover, in the *Rate Order,* the Commission determined that such a la carte packages would be exempt from rate regulation, i.e., would be deemed not to fall within the definition of "cable programming service," if two conditions were met: (1) the price for the combined package must not exceed the sum of the individual charges for each component service; and (2) the cable operator must continue to provide the component parts of the package to subscribers separately in addition to the package. The Commission said that the second condition would be satisfied only when "the per channel offering provides consumers with a realistic service choice."[20]

16. Under the two-part test that we set forth in the *Rate Order,* it is clear, first, that the price for the combined package does not exceed the sum of the individual charges for the four services, because subscribers may purchase any one of the four channels for $.75 each or the four-channel package for $1.50. The second part of the test is whether the separate parts of the package constitute a "realistic service offering." The results of our review of Dimension Cable's submission reveal that only about one percent of its subscribers in Rancho Palos Verdes chosenot to subscribe to the package. Although only 1.5 percent of Dimension Cable's subscribers chose not to purchase the a la carte package, our test does not specify what percentage would indicate that an offering is "a realistic service offering." However, this fact, together with the other factors present in this case,[21] tends to show, in this instance, that the per-channel offering does not constitute a realistic service offering.

17. Even if we were to apply the 15 interpretative guidelines set forth in our *Second Reconsideration Order,*[22] we still would not reach a clear answer to the question of what constitutes a realistic service offering. Although some factors support a finding that Dimension Cable's offering was not a permissible a la carte package, other factors point the other way. In particular, although a "significant percentage" of the channels offered in the a la carte package (100 percent) was removed from a regulated tier, the absolute number (four) was small.[23] Moreover, our test does not explain how the factors are to be weighed against each other. In these circumstances, we cannot say that it was clear to Dimension Cable that its restructuring was not a permissible a la carte package.

18. In our recently adopted *Going Forward Order,* we have reconsidered our rules relating to a la carte packages and concluded that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act. For that reason, the package at issue is subject to rate regulation and cannot continue to be treated as an unregulated package of channels. In reaching this conclusion in the *Going Forward Order,* we acknowledged that, as applied to many fact patterns, we did not provide a clear test in the *Rate Order* and the *Second Reconsideration Order* for determining whether an a la carte package was permissible. In adopting the 15 interpretive guidelines in the *Second Reconsideration Order* to supplement the *Rate Order's* two-prong test, we hoped to enable operators to better determine what collective offerings of a la carte channels would be considered a realistic service offering, and, hence, not an evasion of rate regulation.[24] Our experience to date, however, indicates that our efforts did not produce the intended result and that, instead, there has been confusion as to whether collective offerings of a la carte channels constituted an evasion of rate regulation. Indeed, we cannot say that it is clear that Dimension Cable's restructuring was not a permissible a la carte package.

19. For that reason, we do not think that it would be equitable to subject Dimension Cable to refund liability. This result is distinguishable from the result we reached in *Adelphia Cable Partners, L.P.,*[25] in which we determined that we will require refunds if Adelphia's rate justification proceedings show that subscribers' rates were higher than our rules permitted. In that case, the cable operator announced that it would offer all the channels previously offered on a cable programming service tier on an individual basis or as a collective offering of a la carte channels. In so doing, Adelphia removed an entire service tier from

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Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking, MM Docket Nos. 92-266 and 93-215, FCC 94-286 (adopted November 10, 1994) *("Going Forward Order").* Specifically, we have determined that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act and therefore will be subject to our general rate regulation rules. However, in order to determine whether Dimension Cable evaded rate regulation when it restructured its offering, we must evaluate its a la carte package under the rules that were in effect when it restructured.

[18] *Rate Order* ¶ 329.

[19] *See, e.g., Rate Order* ¶ 453 n.1161 ("There is no evidence that operators would or, as a business matter, could shift programming previously offered as part of a tier to 'a la carte' status, *i.e.,* a per-channel or per-program offering, to avoid the rate regulation applicable to tiers").

[20] *Id.* at ¶ ¶ 327-28 & n.808. In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-266, *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking,* 9 FCC Rcd 4119 (1994) *("Second Reconsideration Order"),* the Commission affirmed its prior view. It said that "we continue to believe that the public interest will be served by generally permitting non-regulated treatment of collective offerings of 'a la carte' channels if the offering enhances consumer choice and does not constitute an evasion of rate regulation." *Id.* at ¶ 194. In this regard, we retained the two-part test contained in the *Rate Order* for determining when we would refrain from regulating "a la carte packages." In addition, the Commission set out 15 guidelines to enable operators to better determine what collective offerings of "a la carte" channels will be considered "realistic service offerings." *Id.* at ¶ 195.

[21] *See, e.g.,* ¶ ¶ 12-13, *supra.*

[22] *Second Reconsideration Order* at ¶ 196.

[23] *Id.*

[24] *See Going Forward Order* ¶ 40.

[25] *Adelphia Cable Partners, L.P.,* South Dade County, Florida, LOI-93-42, FCC 94-1277 (released November 18, 1994).

rate regulation. In contrast, Dimension Cable attempted to treat only four channels as an unregulated collective offering of a la carte channels. Moreover, while we have indicated above that our rules for determining whether collective offerings of a la carte channels constitute an evasion were in many instances difficult to apply, we do not believe that our a la carte rules are unclear as applied to the fact pattern in the *Adelphia* case. In the *Rate Order*, we stated that a cable operator could not escape rate regulation simply by calling what otherwise would be a rate regulated tier an a la carte package.[26] We reiterated this admonition in the *Second Reconsideration Order* when we warned against eliminating "an entire regulated tier" and "turning it into an a la carte package."[27]

20. We will not require Dimension Cable to restructure its tiers so as to return the channels offered in the a la carte package to the basic or standard tiers,[28] instead, on a prospective basis, therefore, we will consider Dimension Cable's collective offering of a la carte channels a new product tier[29] even though it would not qualify as a new product tier under our recently announced *Going Forward Order* because one of the conditions for a new product tier is that channels may not be removed from a basic service tier or a cable programming service tier. In light of the prior confusion over what constituted a permissible a la carte offering, and because Dimension Cable's four-channel tier, unlike Adelphia's offering, did not constitute a clear evasion of our rate rules, we see no good reason to subject Dimension Cable or its Rancho Palos Verdes customers to the confusion and transaction costs that would result if we required Dimension Cable to retier.

V. ORDERING CLAUSES

21. Accordingly, IT IS ORDERED that Dimension Cable's package as it existed on December 13, 1993, may be treated as a new product tier under our *Going Forward Order*.

22. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[26] *Rate Order*, 8 FCC Rcd 5837, n.808 ("we do not think a cable operator can escape rate regulation simply by announcing that tiered services are available a la carte").

[27] *Second Reconsideration Order* ¶ 196.

[28] We are not precluding Dimension Cable from treating this package as a cable programming service tier, priced pursuant to our rules, or from putting the channels back into an existing tier.

[29] *Going Forward Order* ¶ ¶ 16-37.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Dimension Cable Services, Oceanside, California — LOI-93-36

Letter of Inquiry

MEMORANDUM OPINION AND ORDER

Adopted: November 23, 1994; Released: November 25, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. A subscriber of Times Mirror Cable Television of San Diego, Inc., d/b/a Dimension Cable Services ("Dimension Cable"), filed an FCC Form 329 complaint dated October 8, 1993, that alleged violations by Dimension Cable of Commission regulations governing cable television. In response to this complaint, the Commission issued Letter of Inquiry 93-36 ("LOI") to Dimension Cable on December 13, 1993.[1] The LOI asked Dimension Cable to provide information concerning its compliance with the Commission's rules governing evasion in the offering of packages which allegedly are not rate-regulated. Dimension Cable responded to our LOI on January 13, 1994.

II. BACKGROUND

2. In the Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act"), Congress created a regulatory scheme giving the Commission and local franchising authorities jurisdiction over the cable programming and equipment rates of non-competitive cable systems. The 1992 Cable Act provides that the rates of cable systems not subject to effective competition may be regulated by local franchising authorities, in the case of basic service, and by the Commission, in the case of cable programming services.[2] A stated policy of the 1992 Cable Act is to ensure that "consumer interests are protected in the receipt of cable service."[3]

3. The 1992 Cable Act requires cable operators to offer subscribers a basic tier that must contain at least all qualified local broadcast signals and, unless otherwise specified by the local franchising authority, public, educational, and governmental channels.[4] The Commission was charged by the 1992 Cable Act with creating regulations that ensure that the rates for the basic service tier are reasonable.[5] The 1992 Cable Act directs that "[s]uch regulations shall be designed to achieve the goal of protecting subscribers of any cable system that is not subject to effective competition from rates for the basic service tier that exceed the rates that would be charged for the basic service tier if such cable system were subject to effective competition."[6] Under the 1992 Cable Act, operators may offer other channels in a cable programming service tier or tiers.[7] The 1992 Cable Act orders the Commission to create regulations for the cable programming service tiers that allow it to identify individual cases of unreasonable rates.[8] The 1992 Cable Act thus protects consumers' interests in continuing to receive the basic service tier and cable programming service tiers at reasonable rates.

4. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[9] The 1992 Cable Act's legislative history states that the Commission should scrutinize offerings of non-traditional stand-alone services to "prevent repricing, retiering, or other alterations of rate structures" that could have the effect of evading the purposes of rate regulation.[10] This provision in the 1992 Cable Act is intended to give the Commission the authority to address changes in the cable industry's business practices that would thwart the intent of rate regulation.[11]

5. In the *Rate Order* the Commission defined evasion as "any practice or action which avoids the rate regulation provisions of the Cable Act or Commission rules contrary to the intent of the Act or its underlying policies."[12] We must scrutinize a particular operator's marketing or pricing

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[1] Letter from Roy J. Stewart, Chief, Mass Media Bureau, FCC, to Dimension Cable Services, LOI-93-36 (December 13, 1993). Copies of the Letter of Inquiry and Response are available to the public in the FCC's Cable Reference Center, 2033 M Street, N.W., Room 207, Washington, D.C. We also note that there is a pending rate complaint proceeding involving Dimension Cable. Our decisions made herein will be made a part of that proceeding. Thus, for example, we will not order Dimension Cable to make refunds to subscribers in regard to Dimension Cable's purported "a la carte" restructuring. Obviously, however, we may order refunds if we find violations of other rules that should result in refunds.

[2] Communications Act of 1934 § 623 (a)(2), 47 U.S.C. § 543 (a)(2)(1992).

[3] Pub. L. No. 102-385 § 2 (b) (4) (1992); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. at 34 (1992).

[4] Communications Act of 1934 § 623 (b)(7)(A)(ii-iii), 47 U.S.C. § 543 (b)(7)(A)(ii-iii)(1992); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket 92-266, *Report and Order and Further Notice of Proposed Rulemaking*, 8 FCC Rcd 5631 ¶ 157-161 (1993) (*"Rate Order"*) (franchising authorities may require operators to carry PEG channels on tiers other than basic).

[5] Communications Act of 1934 § 623 (b)(1), 47 U.S.C. § 543 (b)(1)(1992).

[6] *Id.*

[7] Communications Act of 1934 § 623(l)(2), 47 U.S.C. § 543(l)(2)(1992).

[8] Communications Act of 1934 § 623 (c)(1)(A), 47 U.S.C. § 543 (c)(1)(A)(1992). Identification of individual cases of unreasonable rates is achieved by a process in which the Commission assumes jurisdiction over systems where a complaint about a cable programming service tier rate is filed.

[9] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[10] H.R. Rep. No. 628, 102d Cong., 2d Sess. at 79 (1992).

[11] S. Rep. No. 92, 102d Cong., 2d Sess. at 77 (1992).

[12] *Rate Order* ¶ 451.

practices to determine whether those practices have the effect of avoiding the requirements of our rate regulations, contrary to the intent of the 1992 Cable Act and our rules.

III. FACTS

6. Before the effective date of the Commission's rate rules, Dimension Cable's services included: an 18 channel basic tier for $14.00; a 23 channel cable programming services tier called Preferred Dimension for $10.20; and five premium channels offeredon a per-channel or package basis. Only customers whose television sets were not capable of receiving all 41 channels needed converters to receive these services. Customers needed addressable converters to subscribe to the five premium channels.

7. The following chart summarizes Dimension Cable's service tier offerings prior to September 1, 1993:

Offering	Channels	Price
1. Basic	18	$14.00
2. Preferred Dimension	23	$10.20
Total	41	$24.20

8. On August 31, 1993, the day before cable rate regulation became effective, Dimension Cable restructured its programming services to add a la carte offerings. It states that it moved four channels, American Movie Classics, Turner Network Television, The Nashville Network and The Discovery Channel, from the Preferred Dimension tier and offered them a la carte at a price of $1.50 each. The four a la carte channels were also sold in a package for $2.95. Its basic tier cost $12.95 and its Dimension cable programming service tier cost $11.20. Only customers who needed converters before the restructuring needed them to receive the a la carte channels. Although waived for the first 30 days, Dimension Cable charges customers for switching among these services.

9. The following chart summarizes Dimension Cable's service tier options as of the date of its response to our LOI:[13]

Offering	Channels	Price
1. Basic	21	$12.95
2. Dimension	18	$11.10
3. Package	27	$2.95
Total	43	$27.00

10. Dimension Cable states that existing customers bought the package at a rate of 97.9 percent. As of January 13, 1994, 71 of Dimension Cable's customers chose to receive one or more individual a la carte channels, while 38,753 subscribed to the package.

IV. DISCUSSION

11. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[14] An evasion, as defined by the Commission, is an act or practice that "avoids the rate regulation provisions of the [Cable] Act or our rules contrary to the intent of the Act or its underlying policies."[15] In the *Rate Order*, we stated that "retiering otherwise permitted under our rules will not be deemed an evasion."[16] First, we examine whether Dimension Cable's response to the LOI shows that its restructuring of its offerings had the effect of evading rate regulation for the channels that Congress intended to be rate-regulated.

12. Dimension Cable's restructuring effective September 1, 1993, involved its movement of four channels (American Movie Classics, Turner Network Television, The Nashville Network and The Discovery Channel) from its 23 channel Preferred Dimension tier to create the four-channel package that it alleges is not rate-regulated. Thus, Dimension Cable removed channels from otherwise rate-regulated tiers to create a new package of channels. In so doing, Dimension Cable avoided application of our rate regulations which generally required cable operators to reduce rates by about 10 percent. That is, if Dimension Cable had not restructured on September 1, 1993, it would have been required to recalculate its rates in accordance with the *Rate Order* we released on May 3, 1993, which generally required cable operators to reduce their rates. Moreover, customers that were receiving the four cable programming service tier channels at issue continued to receive them after the restructuring, and there appears to be no sufficient justification for Dimension Cable's restructuring other than to avoid rate regulation.

13. Other factors corroborate our view that Dimension Cable's restructuring may have had the effect of avoiding rate regulation. First, it offered this package on the eve of regulation. Second, it automatically subscribed its customers to the offerings that previously had been part of its cable programming service tiers. In light of these facts, it appears that Dimension Cable's restructuring of its offerings may have evaded rate regulation. We will not find an actual evasion occurred, however, if Dimension Cable's action complied with our a la carte policy that was in effect at the time of its restructuring. If the offering met our requirements for a permissible collective offering of a la carte channels, then Dimension Cable would not have evaded our rate regulations because it would not be required to reduce its price for the collective a la carte package.[17]

14. In our *Rate Order*, the Commission recognized that "a la carte packages" appear to be "cable programming services," but said that "interpreting the statute in such a literal fashion could disadvantage consumers by denying them discounts on packages of per-channel or per-program

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[13] This Order does not evaluate Dimension Cable's rates for its basic and cable programming service tiers. These rates are subject to review by the local franchising authority and the Commission in separate proceedings.

[14] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[15] *Rate Order* ¶ 451.

[16] *Id.* at ¶ 453.

[17] In our *Going Forward Order*, we have reconsidered our regulatory treatment of collective offerings of a la carte channels. *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking*, MM Docket Nos. 92-266 and 93-215, FCC 94-286 (adopted November 10, 1994) *("Going Forward Order")*. Specifically, we have determined that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act and therefore will be subject to our general rate regulation rules. However, in order to determine whether Dimension Cable evaded rate regulation when it restructured its offering, we must evaluate its a la carte package under the rules that were in effect when it restructured.

services and by limiting subscriber access to a greater quantity of premium programming."[18] Thus, we envisioned that cable operators, for the most part, would offer channels that previously had been offered a la carte in discounted packages, and concluded that it would be better for consumers if we construed the 1992 Cable Act to permit such discounting.[19] This is not the type of offering that Dimension Cable and others have provided their subscribers. Specifically, these operators did not offer a discounted package of channels that previously had been offered a la carte to subscribers, but instead removed channels from a tier that would be subject to our rate regulations.

15. Moreover, in the *Rate Order,* the Commission determined that such a la carte packages would be exempt from rate regulation, i.e., would be deemed not to fall within the definition of "cable programming service," if two conditions were met: (1) the price for the combined package must not exceed the sum of the individual charges for each component service; and (2) the cable operator must continue to provide the component parts of the package to subscribers separately in addition to the package. The Commission said that the second condition would be satisfiedonly when "the per channel offering provides consumers with a realistic service choice."[20]

16. Under the two-part test that we set forth in the *Rate Order,* it is clear, first, that the price for the combined package does not exceed the sum of the individual charges for the four services, because subscribers may purchase any one of the four channels for $1.50 each or the four-channel package for $2.95. The second part of the test is whether the separate parts of the package constitute a "realistic service offering." The results of our review of Dimension Cable's submission reveal that only less than one percent of its subscribers in Oceanside chose not to subscribe to the package. Although only about 2.1% percent of Dimension Cable's subscribers chose not to purchase the a la carte package, our test does not specify what percentage would indicate that an offering is "a realistic service offering." However, this fact, together with the other factors present in this case,[21] tends to show, in this instance, that the per-channel offering does not constitute a realistic service offering.

17. Even if we were to apply the 15 interpretative guidelines set forth in our *Second Reconsideration Order,*[22] we still would not reach a clear answer to the question of what constitutes a realistic service offering. Although some factors support a finding that Dimension Cable's offering was not a permissible a la carte package, other factors point the other way. In particular, although a "significant percentage" of the channels offered in the a la carte package (100 percent) was removed from a regulated tier, the absolute number (four) was small.[23] Moreover, our test does not explain how the factors are to be weighed against each other. In these circumstances, we cannot say that it was clear to Dimension Cable that its restructuring was not a permissible a la carte package.

18. In our recently adopted *Going Forward Order,* we have reconsidered our rules relating to a la carte packages and concluded that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act. For that reason, the package at issue is subject to rate regulation and cannot continue to be treated as an unregulated package of channels. In reaching this conclusion in the *Going Forward Order,* we acknowledged that, as applied to many fact patterns, we did not provide a clear test in the *Rate Order* and the *Second Reconsideration Order* for determining whether an a la carte package was permissible. In adopting the 15 interpretive guidelines in the *Second Reconsideration Order* to supplement the *Rate Order's* two-prong test, we hoped to enable operators to better determine what collective offerings of a la carte channels would be considered a realistic service offering, and, hence, not an evasion of rate regulation.[24] Our experience to date, however, indicates that our efforts did not produce the intended result and that, instead, there has been confusion as to whether collective offerings of a la carte channels constituted an evasion of rate regulation. Indeed, we cannot say that it is clear that Dimension Cable's restructuring was not a permissible a la carte package.

19. For that reason, we do not think that it would be equitable to subject Dimension Cable to refund liability. This result is distinguishable from the result we reached in *Adelphia Cable Partners, L.P.,* South Dade County, Florida, LOI-93-42, in which we determined that we will require refunds if Adelphia's rate justification proceedings show that subscribers' rates were higher than our rules permitted. In that case, the cable operator announced that it would offer all the channels previously offered on a cable programming service tier on an individual basis or as a collective offering of a la carte channels. In so doing, Adelphia removed an entire service tier from rate regulation. In contrast, Dimension Cable attempted to treat only four channels as an unregulated collective offering of a la carte channels. Moreover, while we have indicated above that our rules for determining whether collective offerings of a la carte channels constitute an evasion were in many instances difficult to apply, we do not believe that our a la carte rules are unclear as applied to the fact pattern in the *Adelphia* case. In the *Rate Order,* we stated that a cable

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[18] *Rate Order* ¶ *329.*

[19] *See, e.g., Rate Order* ¶ 453 n.1161 ("There is no evidence that operators would or, as a business matter, could shift programming previously offered as part of a tier to 'a la carte' status, *i.e.,* a per-channel or per-program offering, to avoid the rate regulation applicable to tiers").

[20] *Id.* at ¶ ¶ 327-28 & n.808. In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-266, *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking,* 9 FCC Rcd 4119 (1994) (*"Second Reconsideration Order"),* the Commission affirmed its prior view. It said that "we continue to believe that the public interest will be served by generally permitting non-regulated treatment of collective offerings of 'a la carte' channels if the offering enhances consumer choice and does not constitute an evasion of rate regulation." *Id.* at ¶ 194. In this regard, we retained the two-part test contained in the *Rate Order* for determining when we would refrain from regulating "a la carte packages." In addition, the Commission set out 15 guidelines to enable operators to better determine what collective offerings of "a la carte" channels will be considered "realistic service offerings." *Id.* at ¶ 195.§

[21] *See, e.g.,* ¶ ¶ 12-13, *supra.*

[22] *Second Reconsideration Order* at ¶ 196.

[23] *Id.*

[24] *See Going Forward Order* at ¶ 40.

operator could not escape rate regulation simply by calling what otherwise would be a rate regulated tier an a la carte package.[25] We reiterated this admonition in the *Second Reconsideration Order* when we warned against eliminating "an entire regulated tier" and "turning it into an a la carte package."[26]

20. We will not require Dimension Cable to restructure its tiers so as to return the channels offered in the a la carte package to the basic or standard tiers,[27] instead, on a prospective basis, therefore, we will consider Dimension Cable's collective offering of a la carte channels a new product tier[28] even though it would not qualify as a new product tier under our recently announced *Going Forward Order* because one of the conditions for a new product tier is that channels may not be removed from a basic service tier or a cable programming service tier. In light of the prior confusion over what constituted a permissible a la carte offering, and because Dimension Cable's four-channel tier, unlike Adelphia's offering, did not constitute a clear evasion of our rate rules, we see no good reason to subject Dimension Cable or its Oceanside customers to the confusion and transaction costs that would result if we required Dimension Cable to retier.

V. ORDERING CLAUSES

21. Accordingly, IT IS ORDERED that Dimension Cable's package as it existed on December 13, 1993, may be treated as a new product tier under our *Going Forward Order*.

22. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[25] *Rate Order*, 8 FCC Rcd 5837, n.808 ("we do not think a cable operator can escape rate regulation simply by announcing that tiered services are available a la carte").

[26] *Second Reconsideration Order* ¶ 196.

[27] We are not precluding Dimension Cable from treating this package as a cable programming service tier, priced pursuant to our rules, or from putting the channels back into an existing tier.

[28] *Going Forward Order* ¶ ¶ 16-37.

Before the
Federal Communications Commission
Washington, D.C. 20554

MM Docket No. 94-143

In the Matter of

Amendment of Section 73.606(b).
Table of Allotments.
Television Broadcast Stations.
(Albion, Nebraska)

NOTICE OF PROPOSED RULE MAKING

Adopted: December 1, 1994; Released: December 5, 1994

Comment Date: February 13, 1995
Reply Comment Date: February 28, 1995

By the Acting Chief, Allocations Branch:

1. The Commission, on its own motion, proposes to allot UHF Channel 24 to Albion, Nebraska, in order to permit Citadel Communications Co., Inc. ("Citadel Communications") to amend its pending mutually exclusive application (File No. BPCT-930726KH) for Channel 18 in Albion, to specify operation on Channel 24.[1] In the event any interested party expresses a timely interest in a UHF allotment in Albion, we are prepared to allot Channel 40 to accommodate this interest.

BACKGROUND

2. Citadel Communications is the licensee of television Station KCAN, Channel 8, Albion, Nebraska.[2] In *Albion, Lincoln, and Columbus, Nebraska*, 6 FCC Rcd 2876 (1993), we substituted UHF Channel 18 for VHF Channel 8 at Albion, allotted VHF Channel 8 to Lincoln, and modified the Citadel Communications Station KCAN license to specify Lincoln as the community of license. That action was specifically premised on the pledge of Citadel Communications to file an application for Channel 18 in Albion and operate it as a satellite of Station KCAU.

3. Fant Broadcasting of Nebraska, Inc. filed a competing application for the Channel 18 allotment in Albion proposing a full-service facility (File No. BPCT-931115KF). At the present time, there is no basis upon which to designate these applications for a comparative hearing or to otherwise resolve these mutually exclusive applications. *See Bechtel v. Federal Communications Commission*, 10 F3d 875 (D.C. Cir. 1993).

4. In regard to the underlying Channel 18 allotment, the *Notice* in *Albion, Lincoln, and Columbus, Nebraska, supra*, specifically stated that Channel 18 was being proposed in order to allow Citadel Communications to continue its existing ABC network affiliated satellite service to Albion. 6 FCC Rcd 6038 (1991). Had Fant Broadcasting expressed an interest in operating a full-service station in Albion, we would have allotted an additional channel to accommodate that expression of interest. *See, e.g., Roseburg, Oregon* 6 FCC Rcd 4369 (1991). *Cf. Copeland, Kansas*, 5 FCC Rcd 7682 (1990); *Lander, Wyoming*, 46 FR 39605 (August 4, 1981); *West Palm Beach, Florida*, 46 RR2d 1272 (1980); *Rapid City, South Dakota*, 6 FCC Rcd 4471 (1991). At this juncture, we see no public interest benefit in delaying resolution of the Albion proceeding. On the contrary, we believe that resolving this matter as quickly as possible and providing Albion with its first full-service television station, providing a second television service in Albion and retaining ABC network-affiliated satellite service provide overriding public interest benefits. For these reasons, we propose to allot Channel 24 to Albion and permit Citadel Communications to amend its pending application for Channel 18 to specify operation on Channel 24 without loss of cut-off protection.

5. In view of the above and the fact that the proposed allotment would provide a second television service to Albion, Nebraska, we propose to amend the TV Table of Allotments, Section 73.606(b) of the Commission's Rules, with respect to the following community:

	Channel No.	
City	Present	Proposed
Albion, Nebraska	18,[3] *21+	18, *21+, 24

6. The Commission's authority to institute rule making proceedings, showings required, cut-off procedures, and filing requirements are contained in the attached Appendix and are incorporated by reference herein.

7. Interested parties may file comments on or before **February 13, 1995,** and reply comments on or before **February 28, 1995,** and are advised to read the Appendix for the proper procedure. Additionally, a copy of such comments should be served on the applicants for the Channel 18 allotment at Albion, as follows:

Fant Broadcasting of Nebraska, Inc.
c/o Fletcher, Heald & Hildreth
1300 North 17th St.
Rosslyn, Virginia 22209

Citadel Communications Co., Inc.
c/o Latham & Watkins
1001 Pennsylvania Avenue, NW
Washington, D.C. 20004

[1] The reference coordinates for Channel 24 at Albion, Nebraska, are 41-55-48 and 98-17-23.

[2] Citadel Communications operates Station KCAN in Albion as a satellite of commonly owned television Station KCAU, Channel 9, Sioux City, Iowa. Station KCAU is an ABC network affiliate.

[3] Channel 18 was reallotted from Albion to Lincoln, Nebraska, in *Albion, Lincoln, and Columbus, Nebraska, supra*. In view of the fact that Pappas Telecasting of the Midlands and Busse Broadcasting Corporation have filed petitions for reconsideration directed to that action, the reallotment is not final.

8. The Commission has determined that the relevant provisions of the Regulatory Flexibility Act of 1980 do not apply to a rule making proceeding to amend the TV Table of Allotments, Section 73.606(b) of the Commission's Rules. *See Certification that Sections 603 and 604 of the Regulatory Flexibility Act Do Not Apply to Rule Making to Amend Sections 73.202(b), 73.504 and 73.606(b) of the Commission's Rules.* 46 FR 11549 (February 9, 1981).

9. For further information concerning this proceeding, contact Robert Hayne, Mass Media Bureau, (202) 634-6530. For purposes of this restricted notice and comment rule making proceeding, members of the public are advised that no *ex parte* presentations are permitted from the time the Commission adopts a Notice of Proposed Rule Making until the proceeding has been decided and such decision is no longer subject to reconsideration by the Commission or review by any court. An *ex parte* presentation is not prohibited if specifically requested by the Commission or staff for the clarification or adduction of evidence or resolution of issues in the proceeding. However, any new written information elicited from such a request or a summary of any new information shall be served by the person by theH& person making the presentation upon the other parties to the proceeding unless the Commission specifically waives this service requirement. Any comment which has not been served on the petitioner constitutes an *ex parte* presentation and shall not be considered in the proceeding. Any reply comment which has not been served on the person(s) who filed the comment, to which the reply is directed constitutes an *ex parte* presentation and shall not be considered in the proceeding.

FEDERAL COMMUNICATIONS COMMISSION

John A. Karousos
Acting Chief, Allocations Branch
Policy and Rules Division
Mass Media Bureau

APPENDIX

1. Pursuant to authority contained in Sections 4(i), 5(c)(1),303(g) and (r) and 307(b) of the Communications Act of 1934, as amended, and Sections 0.61 0.204(b) and 0.283 of the Commission's Rules, IT IS PROPOSED TO AMEND the FM Table of Allotments, Section 73.202(b) of the Commission's Rules and Regulations, as set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached.

2. *Showings Required.* Comments are invited on the proposal(s) discussed in the *Notice of Proposed Rule Making* to which this Appendix is attached. Proponent(s) will be expected to answer whatever questions are presented in initial comments. The proponent of a proposed allotment is also expected to file comments even if it only resubmits or incorporates by reference its former pleadings. It should also restate its present intention to apply for the channel if it is allotted and, if authorized, to build a station promptly. Failure to file may lead to denial of the request.

3. *Cut-off Procedures.* The following procedures will govern the consideration of filings in this proceeding.

(a) Counterproposals advanced in this proceeding itself will be considered if advanced in initial comments, so that parties may comment on them in reply comments. They will not be considered if advanced in reply comments. *(See* Section 1.420(d) of the Commission's Rules.)

(b) With respect to petitions for rule making which conflict with the proposal(s) in this *Notice,* they will be considered as comments in the proceeding, and Public Notice to this effect will be given as long as they are filed before the date for filing initial comments herein. If they are filed later than that, they will not be considered in connection with the decision in this docket.

(c) The filing of a counterproposal may lead the Commission to allot a different channel than was requested for any of the communities involved.

4. *Comments and Reply Comments; Service.* Pursuant to applicable procedures set out in Sections 1.415 and 1.420 of the Commission's Rules and Regulations, interested parties may file comments and reply comments on or before the dates set forth in the *Notice of Proposed Rule Making* to which this Appendix is attached. All submissions by parties to this proceeding or by persons acting on behalf of such parties must be made in written comments, reply comments, or other appropriate pleadings. Comments shall be served on the petitioner by the person filing the comments. Reply comments shall be served on the person(s) who filed comments to which the reply is directed. Such comments and reply comments shall be accompanied by a certificate of service. *(See* Section 1.420(a), (b) and (c) of the Commission's Rules.) Comments should be filed with the Secretary, Federal Communications Commission, Washington, D.C. 20554.

5. *Number of Copies.* In accordance with the provisions of Section 1.420 of the Commission's Rules and Regulations, an original and four copies of all comments, reply comments, pleadings, briefs, or other documents shall be furnished the Commission.

6. *Public Inspection of Filings.* All filings made in this proceeding will be available for examination by interested parties during regular business hours in the Commission's Public Reference Room at its headquarters, 1919 M Street N.W., Washington, D.C.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

C-TEC CABLE SYSTEMS
OF MICHIGAN, INC.

Petition for Reconsideration

of the Certification of
Everett Township, Michigan
to Regulate Basic Cable Rates
(MI0935)

MEMORANDUM OPINION AND ORDER

Adopted: November 29, 1994; Released: December 2, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On November 15, 1993, C-TEC Cable Systems of Michigan, Inc. ("C-TEC") filed a timely petition for reconsideration challenging the certification of Everett Township, Michigan to regulate rates for basic cable service and associated equipment.[1] Everett Township filed an objection. In addition, C-TEC submitted a supplement providing documentation in support of its petition pursuant to a recent Commission Order.[2]

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[3] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[4] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[5] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[6] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[7]

II. DISCUSSION

3. C-TEC argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in Everett Township, the franchise area.[8] The supplement to C-TEC's petition shows that the cable system currently serves only nine of the 530 households (that is, occupied housing units)[9] in the franchise area, or 1.7 percent of the total number of households. As supporting documentation, C-TEC provides 1990 Census data[10] which shows that there are 530 occupied housing units in Everett Township. C-TEC also submits a computer printout with sufficient subscriber information to show that it serves nine households in the franchise area.

4. In response, Everett Township argues that C-TEC has made an affirmative decision to limit its actual service area to a more densely populated sector of the Township. Everett Township claims that, as a result, C-TEC has redefined the franchise area for purposes of the effective competition standard.[11] Everett does not submit a copy of

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[1] Everett Township filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") on October 14, 1993, which became effective on November 13, 1993.

[2] *Cable Operators' Petition for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994) ("*Effective Competition Order*").

[3] 47 U.S.C. § 543(a)(4).

[4] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[5] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition.47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[6] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[7] 47 C.F.R. § 76.911(c).

[8] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30% of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[9] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) ("*Third Recon. Order*"). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[10] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Effective Competition Order, supra.*

[11] In the *First Order on Reconsideration*, the Commission clarified the definition of "franchise area" for purposes of determining effective competition. *First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking*, MM Docket No. 92-266, 9 FCC Rcd 1164 (1993). Generally, "[a] franchise area is the area a system operator is granted authority to serve in its franchise." *Id.* at 1180. The Commission stated, however, that a more restricted definition of "franchise area" may be appropriate under limited circumstances, such as when an operator "has itself, through its own conduct, self-defined the areas to be served to such an extent that this redefined area accurately portrays the operator's 'fran-

its franchise agreement with C-TEC, a map indicating C-TEC's service area, complaints of C-TEC sfailure to expand its service area or any other documentation to support its claim.

5. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[12] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[13] C-TEC has met this burden.

6. As a preliminary matter, we are unpersuaded that the appropriate franchise area for purposes of effective competition is something less than the entire Everett Township. Everett Township provides no evidence to support its argument that C-TEC has made an affirmative decision to limit its service to a more densely populated area within the Township. Thus, we find that Everett Township has failed to sustain its burden of proof that C-TEC has redefined its franchise area.

7. C-TEC appropriately relied on data reflecting the number of households as required by our rules.[14] Relying on this data, C-TEC has submitted sufficient evidence demonstrating that its cable system serving Everett Township, its franchise area, serves nine of the 530 households, or 1.7 percent of the households, within its franchise area.[15] Thus, we find C-TEC's system serving Everett Township is subject to effective competition. Accordingly, its petition is granted.

III. ORDERING CLAUSES

8. Accordingly, IT IS ORDERED that the petition for reconsideration filed by C-TEC challenging the certification of Everett Township to regulate basic cable rates IS GRANTED.

9. IT IS FURTHER ORDERED that the certification of Everett Township to regulate C-TEC's basic cable rates IS RESCINDED.

10. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

chise area.'" *Id.* at 1181. Under this standard, the franchising authority has the burden of showing that the operator has made an "affirmative decision . . . to restrict service." *Id.*

[12] 47 C.F.R. § 76.906.

[13] 47 C.F.R. § 76.911(b)(1).

[14] *Third Recon. Order, supra.*

[15] Initially, C-TEC stated that there were 796 "homes" in its franchise area. This data was apparently based on housing unit data which includes both occupied and vacant housing units. In its supplement, however, C-TEC submits household data which indicates that there are 530 occupied housing units in Everett Township. As C-TEC's supplement contains the correct information, we will rely on it for purposes of reviewing this petition.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

C-TEC CABLE SYSTEMS
OF MICHIGAN, INC.

Petition for Reconsideration

of the Certification of
Cleveland Township, Michigan
to Regulate Basic Cable Rates
(MI0949)

MEMORANDUM OPINION AND ORDER

Adopted: November 29, 1994; Released: December 2, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. On November 5, 1993, C-TEC Cable Systems of Michigan, Inc. ("C-TEC") filed a timely petition for reconsideration challenging the certification of Cleveland Township, Michigan to regulate rates for basic cable service and associated equipment.[1] In addition, C-TEC submitted a supplement providing documentation in support of its petition pursuant to a recent Commission Order.[2] Cleveland Township did not file an opposition to C-TEC's petition.

2. Section 623(a)(4) of the Communications Act of 1934, as amended, allows franchising authorities to become certified to regulate basic cable service rates of cable operators that are not subject to effective competition.[3] For purposes of the initial request for certification, local franchising authorities may rely on a presumption that cable operators within their jurisdiction are not subject to effective competition, unless they have actual knowledge to the contrary.[4] Certification becomes effective 30 days from the date of filing unless the Commission finds that the franchising authority does not meet the statutory certification requirements.[5] Cable operators may file petitions for reconsideration of the franchising authority's certification within 30 days from the date such certification becomes effective.[6] Rate regulation is automatically stayed pending review of a timely-filed petition for reconsideration alleging the presence of effective competition.[7]

II. DISCUSSION

3. C-TEC argues that its cable system is subject to effective competition because it serves fewer than 30 percent of the households in Cleveland Township, its franchise area.[8] The supplement to C-TEC's petition shows that the cable system currently serves only 12 of the 300 households (that is, occupied housing units)[9] in the franchise area, or 4 percent of the total number of households. As supporting documentation, C-TEC provides 1990 Census data[10] which shows that there are 300 occupied housing units in Cleveland Township. C-TEC also submits a computer print-out with sufficient subscriber information to show that it serves 12 households in the franchise area.

4. In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[11] The cable operator bears the burden of rebutting the presumption that effective competition does not exist with evidence that effective competition, as defined by Section 76.905 of the Commission's Rules, is present within the franchise area.[12] C-TEC has met this burden. C-TEC appropriately relied on data reflecting the number of households as required by our rules.[13] Relying on this data, C-TEC has submitted sufficient evidence demonstrating that its cable system serving Cleveland Township, its franchise area, serves twelve of the 300 households, or 4 percent of the households, within its franchiseh area.[14]

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[1] Cleveland Township filed its "Certification of Franchising Authority to Regulate Basic Cable Service Rates and Initial Finding of Lack of Effective Competition" ("FCC Form 328") for the franchise area designated as MI0949 on October 13, 1993, which became effective on November 12, 1993.

[2] *Cable Operators' Petition for Reconsideration and Revocation of Franchising Authorities' Certifications to Regulate Basic Cable Service Rates*, 9 FCC Rcd 3656 (1994) (*"Effective Competition Order"*).

[3] 47 U.S.C. § 543(a)(4).

[4] 47 C.F.R. §§ 76.906, 76.910(b)(4).

[5] 47 C.F.R. § 76.910(e). Certification becomes effective unless the Commission determines that: 1) the franchising authority will not adopt and administer rate regulations that are consistent with the Commission's regulations; 2) the franchising authority lacks the legal authority to adopt, or the personnel to administer, rate regulations; 3) procedural laws and regulations applicable to rate regulation proceedings by the franchising authority do not provide a reasonable opportunity for consideration of the views of interested parties; or 4) the cable system in question is subject to effective competition.47 C.F.R. § 76.910(b). *See also* 47 U.S.C. § 543(a)(4).

[6] 47 C.F.R. §§ 1.106, 76.911; *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266, 8 FCC Rcd 5631, 5693 (1993).

[7] 47 C.F.R. § 76.911(c).

[8] The Commission's rules provide that only the rates of cable systems that are not subject to effective competition may be regulated. The Commission's rules further provide that a cable system is subject to effective competition if fewer than 30 percent of the households in the system's franchise area subscribe to the system's service. 47 C.F.R. § 76.905(a) and (b)(1).

[9] As the Commission stated recently, "we presume that Congress did not intend households' to have a different meaning than in the 1990 Census that would include vacant units." *Third Order on Reconsideration*, MM Docket Nos. 92-266 and 92-262, 9 FCC Rcd 4316, 4324 (1994) (*"Third Recon. Order"*). The count of "households" in the 1990 Census reflects only occupied housing units. *See* Bureau of the Census, Dept. of Commerce, 1990 Census of Population, CP-1-1B, Appendix B at B-8.

[10] As the Commission has stated recently, the 1990 Census data is an appropriate source for household data. *Effective Competition Order, supra.*

[11] 47 C.F.R. § 76.906.

[12] 47 C.F.R. § 76.911(b)(1).

[13] *Third Recon. Order, supra.*

[14] PInitially, C-TEC stated that there were 602 "homes" in its franchise area. This data was apparently based on housing unit

Thus, we find C-TEC's system serving Cleveland Township is subject to effective competition. Accordingly, its petition is granted.

III. ORDERING CLAUSES

5. Accordingly, IT IS ORDERED that the petition for reconsideration filed by C-TEC challenging the certification of Cleveland Township to regulate basic cable rates IS GRANTED.

6. IT IS FURTHER ORDERED that the certification of Cleveland Township to regulate C-TEC's basic cable rates IS RESCINDED.

7. This action is taken pursuant to delegated authority pursuant to Section 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

data which includes both occupied and vacant housing units. In its supplement, however, C-TEC submits household data which indicates that there are 300 occupied housing units in Cleveland Township. As C-TEC's supplement contains the correct information, we will rely on it for purposes of reviewing this petition.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Dimension Cable Services, Phoenix, Arizona — LOI-93-30

Letter of Inquiry

MEMORANDUM OPINION AND ORDER

Adopted: November 23, 1994; Released: November 25, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. Subscribers of American Cable Television, Inc., d/b/a Dimension Cable Services ("Dimension Cable"), filed an FCC Form 329 complaint dated October 21, 1993, that alleged violations by Dimension Cable of Commission regulations governing cable television. In response to this complaint, the Commission issued Letter of Inquiry 93-30 ("LOI") to Dimension Cable on December 13, 1993.[1] The LOI asked Dimension Cable to provide information concerning its compliance with the Commission's rules governing evasion in the offering of packages which allegedly are not rate-regulated. Dimension Cable responded to our LOI on January 13, 1994.

II. BACKGROUND

2. In the Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act"), Congress created a regulatory scheme giving the Commission and local franchising authorities jurisdiction over the cable programming and equipment rates of non-competitive cable systems. The 1992 Cable Act provides that the rates of cable systems not subject to effective competition may be regulated by local franchising authorities, in the case of basic service, and by the Commission, in the case of cable programming services.[2] A stated policy of the 1992 Cable Act is to ensure that "consumer interests are protected in the receipt of cable service."[3]

3. The 1992 Cable Act requires cable operators to offer subscribers a basic tier that must contain at least all qualified local broadcast signals and, unless otherwise specified by the local franchising authority, public, educational, and governmental channels.[4] The Commission was charged by the 1992 Cable Act with creating regulations that ensure that the rates for the basic service tier are reasonable.[5] The 1992 Cable Act directs that "[s]uch regulations shall be designed to achieve the goal of protecting subscribers of any cable system that is not subject to effective competition from rates for the basic service tier that exceed the rates that would be charged for the basic service tier if such cable system were subject to effective competition."[6] Under the 1992 Cable Act, operators may offer other channels in a cable programming service tier or tiers.[7] The 1992 Cable Act orders the Commission to create regulations for the cable programming service tiers that allow it to identify individual cases of unreasonable rates.[8] The 1992 Cable Act thus protects consumers' interests in continuing to receive the basic service tier and cable programming service tiers at reasonable rates.

4. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[9] The 1992 Cable Act's legislative history states that the Commission should scrutinize offerings of non-traditional stand-alone services to "prevent repricing, retiering, or other alterations of rate structures" that could have the effect of evading the purposes of rate regulation.[10] This provision in the 1992 Cable Act is intended to give the Commission the authority to address changes in the cable industry's business practices that would thwart the intent of rate regulation.[11]

5. In the *Rate Order* the Commission defined evasion as "any practice or action which avoids the rate regulation provisions of the Cable Act or Commission rules contrary to the intent of the Act or its underlying policies."[12] We must scrutinize a particular operator's marketing or pricing

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[1] Letter from Roy J. Stewart, Chief, Mass Media Bureau, FCC, to Dimension Cable Services, LOI-93-30 (December 13, 1993). Copies of the Letter of Inquiry and Response are available to the public in the FCC's Cable Reference Center, 2033 M Street, N.W., (Room 207, Washington, D.C. We also note that there is a pending rate complaint proceeding involving Dimension Cable. Our decision made herein will be made a part of that proceeding. Thus, for example, we will not order Dimension Cable to make refunds to subscribers in regard to Dimension Cable's purported "a la carte" restructuring. Obviously, however, we may order refunds if we find violations of other rules that should result in refunds.

[2] Communications Act of 1934 § 623 (a)(2), 47 U.S.C. § 543 (a)(2)(1992).

[3] Pub. L. No. 102-385 § 2 (b) (4) (1992); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. at 34 (1992).

[4] Communications Act of 1934 § 623 (b)(7)(A)(ii-iii), 47 U.S.C. § 543 (b)(7)(A)(ii-iii)(1992); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket 92-266, *Report and Order and Further Notice of Proposed Rulemaking*, 8 FCC Rcd 5631 ¶ 157-161 (1993) (*"Rate Order"*) (franchising authorities may require operators to carry PEG channels on tiers other than basic).

[5] Communications Act of 1934 § 623 (b)(1), 47 U.S.C. § 543 (b)(1)(1992).

[6] *Id.*

[7] Communications Act of 1934 § 623(l)(2), 47 U.S.C. § 543(l)(2)(1992).

[8] Communications Act of 1934 § 623 (c)(1)(A), 47 U.S.C. § 543 (c)(1)(A)(1992). Identification of individual cases of unreasonable rates is achieved by a process in which the Commission assumes jurisdiction over systems where a complaint about a cable programming service tier rate is filed.

[9] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[10] H.R. Rep. No. 628, 102d Cong., 2d Sass. at 79 (1992).

[11] S. Rep. No. 92, 102d Cong., 2d Sass. at 77 (1992).

[12] *Rate Order* ¶ 451.

practices to determine whether those practices have the effect of avoiding the requirements of our rate regulations, contrary to the intent of the 1992 Cable Act and our rules.

III. FACTS

6. Before the effective date of the Commission's rate rules, Dimension Cable's services included: a 16 channel basic tier for $10.95; a 7 channel cable programming services tier called Dimension level for $4.80; a 14 channel cable programming services tier called Preferred Dimension for $6.45; and five premium channels offered on a per-channel or package basis. Only customers whose television sets were not capable of receiving all 37 channels needed converters to receive these services. Customers needed addressable converters to subscribe to the five premium channels.

7. The following chart summarizes Dimension Cable's service tier offerings prior to September 1, 1993:

Offering	Channels	Price
1. Basic	16	$10.95
2. Dimension	7	$4.80
3. Preferred Dimension	14	$6.45
Total	37	$22.20

8. On August 31, 1993, the day before cable rate regulation became effective, Dimension Cable restructured its programming services to add a la carte offerings. It states that it moved four channels, American Movie Classics, Turner Network Television, The Nashville Network and The Discovery Channel, from the Preferred Dimension tier and offered them a la carte at a price of $1.23 each. The four a la carte channels were also sold in a package for $2.46. Dimension Cable's restructuring also included the consolidation of its two cable programming services tiers into one cable programming service tier. Its basic tier cost $9.90 and its new Dimension cable programming service tier cost $10.52. Only customers who needed converters before the restructuring needed them to receive the a la carte channels. Although waived for the first 30 days, Dimension Cable charges customers for switching among these services.

9. The following chart summarizes Dimension Cable's service tier options as of the date of its response to our LOI:[13]

Offering	Channels	Price
1. Basic	16	$9.90
2. Dimension	17	$10.52
3. Package	4	$2.46
Total	37	$22.88

10. Dimension Cable states that existing customers bought the package at a rate of 98.9 percent. As of January 13, 1994, 73 of Dimension Cable's customers chose to receive one or more individual a la carte channels while 174,851 subscribed to the package.

IV. DISCUSSION

11. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[14] An evasion, as defined by the Commission, is an act or practice that "avoids the rate regulation provisions of the [Cable] Act or our rules contrary to the intent of the Act or its underlying policies."[15] In the *Rate Order*, we stated that "retiering otherwise permitted under our rules will not be deemed an evasion."[16] First, we examine whether Dimension Cable's response to the LOI shows that its restructuring of its offerings had the effect of evading rate regulation for the channels that Congress intended to be rate-regulated.

12. Dimension Cable's restructuring effective September 1, 1993, involved its movement of four channels (American Movie Classics, Turner Network Television, The Nashville Network and The Discovery Channel) from its 14 channel Preferred Dimension tier to create the four-channel package that it alleges is not rate-regulated. Thus, Dimension Cable removed channels from otherwise rate-regulated tiers to create a new package of channels. In so doing, Dimension Cable avoided application of our rate regulations which generally required cable operators to reduce rates by about 10 percent. That is, if Dimension Cable had not restructured on September 1, 1993, it would have been required to recalculate its rates in accordance with the *Rate Order* we released on May 3, 1993, which generally required cable operators to reduce their rates. Moreover, customers that were receiving the four cable programming service tier channels at issue continued to receive them after the restructuring, and there appears to be no sufficient justification for Dimension Cable's restructuring other than to avoid rate regulation.

13. Other factors corroborate our view that Dimension Cable's restructuring may have had the effect of avoiding rate regulation. First, it offered this package on the eve of regulation. Second, it automatically subscribed its customers to the offerings that previously had been part of its cable programming service tiers. In light of these facts, it appears that Dimension Cable's restructuring of its offerings may have evaded rate regulation. We will not find an actual evasion occurred, however, if Dimension Cable's action complied with our a la carte policy that was in effect at the time of its restructuring. If the offering met our requirements for a permissible collective offering of a la carte channels, then Dimension Cable would not have evaded our rate regulations because it would not be required to reduce its price for the collective a la carte package.[17]

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[13] This Order does not evaluate Dimension Cable's rates for its basic and cable programming service tiers. These rates are subject to review by the local franchising authority and the Commission in separate proceedings.

[14] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[15] *Rate Order* ¶ 451.

[16] *Id.* at ¶ 453.

[17] In our *Going Forward Order*, we have reconsidered our regulatory treatment of collective offerings of a la carte channels. *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Sixth Order on*

14. In our *Rate Order,* the Commission recognized that "a la carte packages" appear to be "cable programming services," but said that "interpreting the statute in such a literal fashion could disadvantage consumers by denying them discounts on packages of per-channel or per-program services and by limiting subscriber access to a greater quantity of premium programming."[18] Thus, we envisioned that cable operators, for the most part, would offer channels that previously had been offered a la carte in discounted packages, and concluded that it would be better for consumers if we construed the 1992 Cable Act to permit such discounting.[19] This is not the type of offering that Dimension Cable and others have provided their subscribers. Specifically, these operators did not offer a discounted package of channels that previously had been offered a la carte to subscribers, but instead removed channels from a tier that would be subject to our rate regulations.

15. Moreover, in the *Rate Order,* the Commission determined that such a la carte packages would be exempt from rate regulation, i.e., would be deemed not to fall within the definition of "cable programming service," if two conditions were met: (1) the price for the combined package must not exceed the sum of the individual charges for each component service; and (2) the cable operator must continue to provide the component parts of the package to subscribers separately in addition to the package. The Commission said that the second condition would be satisfied only when "the per channel offering provides consumers with a realistic service choice."[20]

16. Under the two-part test that we set forth in the *Rate Order,* it is clear, first, that the price for the combined package does not exceed the sum of the individual charges for the four services, because subscribers may purchase any one of the four channels for $1.23 each or the four-channel package for $2.46 The second part of the test is whether the separate parts of the package constitute a "realistic service offering." The results of our review of Dimension Cable's submission reveal that only about one percent of its subscribers in Phoenix chose not to subscribe to the package. Although only 1.1 percent of Dimension Cable's subscribers chose not to purchase the a la carte package, our test does not specify what percentage would indicate that an offering is "a realistic service offering." However, this fact, together with the other factors present in this case,[21] tends to show, in this instance, that the per-channel offering does not constitute a realistic service offering.

17. Even if we were to apply the 15 interpretative guidelines set forth in our *Second Reconsideration Order,*[22] we still would notp reach a clear answer to the question of what constitutes a realistic service offering. Although some factors support a finding that Dimension Cable's offering was not a permissible a la carte package, other factors point the other way. In particular, although a "significant percentage" of the channels offered in the a la carte package (100 percent) was removed from a regulated tier, the absolute number (four) was small.[23] Moreover, our test does not explain how the factors are to be weighed against each other. In these circumstances, we cannot say that it was clear to Dimension Cable that its restructuring was not a permissible a la carte package.

18. In our recently adopted *Going Forward Order,* we have reconsidered our rules relating to a la carte packages and concluded that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act. For that reason, the package at issue is subject to rate regulation and cannot continue to be treated as an unregulated package of channels. In reaching this conclusion in the *Going Forward Order,* we acknowledged that, as applied to many fact patterns, we did not provide a clear test in the *Rate Order* and the *Second Reconsideration Order* for determining whether an a la carte package was permissible. In adopting the 15 interpretive guidelines in the *Second Reconsideration Order* to supplement the *Rate Order's* two-prong test, we hoped to enable operators to better determine what collective offerings of a la carte channels would be considered a realistic service offering, and, hence, not an evasion of rate regulation.[24] Our experience to date, however, indicates that our efforts did not produce the intended result and that, instead, there has been confusion as to whether collective offerings of a la carte channels constituted an evasion of rate regulation. Indeed, we cannot say that it is clear that Dimension Cable's restructuring was not a permissible a la carte package.

19. For that reason, we do not think that it would be equitable to subject Dimension Cable to refund liability. This result is distinguishable from the result we reached in *Adelphia Cable Partners, L.P.,* South Dade County, Florida, LOI-93-42, in which we determined that we will require

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Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking, MM Docket Nos. 92-266 and 93-215, FCC 94-286 (adopted November 10, 1994) *("Going Forward Order").* Specifically, we have determined that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act and therefore will be subject to our general rate regulation rules. However, in order to determine whether Dimension Cable evaded rate regulation when it restructured its offering, we must evaluate its a la carte package under the rules that were in effect when it restructured.

[18] *Rate Order* ¶ *329.*

[19] *See, e.g., Rate Order* ¶ 453 n.1161 ("There is no evidence that operators would or, as a business matter, could shift programming previously offered as part of a tier to 'a la carte' status, *i.e.,* a per-channel or per-program offering, to avoid the rate regulation applicable to tiers").

[20] *Id.* at ¶ ¶ 327-28 & n.808. In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-266, *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking,* 9 FCC Rcd 4119 (1994) *("Second Reconsideration Order"),* the Commission affirmed its prior view. It said that "we continue to believe that the public interest will be served by generally permitting non-regulated treatment of collective offerings of 'a la carte' channels if the offering enhances consumer choice and does not constitute an evasion of rate regulation." *Id.* at ¶ 194. In this regard, we retained the two-part test contained in the *Rate Order* for determining when we would refrain from regulating "a la carte packages." In addition, the Commission set out 15 guidelines to enable operators to better determine what collective offerings of "a la carte" channels will be considered "realistic service offerings." *Id.* at ¶ 195.

[21] *See, e.g.,* ¶ ¶ 12-13, *supra.*

[22] *Second Reconsideration Order* at ¶ 196.

[23] *Id.*

[24] *See Going Forward Order* ¶ 40.

refunds if Adelphia's rate justification proceedings show that subscribers' rates were higher than our rules permitted. In that case, the cable operator announced that it would offer all the channels previously offered on a cable programming service tier on an individual basis or as a collective offering of a la carte channels. In so doing, Adelphia removed an entire service tier from rate regulation. In contrast, Dimension Cable attempted to treat only four channels as an unregulated collective offering of a la carte channels. Moreover, while we have indicated above that our rules for determining whether collective offerings of a la carte channels constitute an evasion were in many instances difficult to apply, we do not believe that our a la carte rules are unclear as applied to the fact pattern in the *Adelphia* case. In the *Rate Order*, we stated that a cable operator could not escape rate regulation simply by calling what otherwise would be a rate regulated tier an a la carte package.[25] We reiterated this admonition in the *Second Reconsideration Order* when we warned against eliminating "an entire regulated tier" and "turning it into an a la carte package."[26]

20. We will not require Dimension Cable to restructure its tiers so as to return the channels offered in the a la carte package to the basic or standard tiers,[27] instead, on a prospective basis, therefore, we will consider Dimension Cable's collective offering of a la carte channels a new product tier[28] even though it would not qualify as a new product tier under our recently announced *Going Forward Order* because one of the conditions for a new product tier is that channels may not be removed from a basic service tier or a cable programming service tier. In light of the prior confusion over what constituted a permissible a la carte offering, and because Dimension Cable's four-channel tier, unlike Adelphia's offering, did not constitute a clear evasion of our rate rules, we see no good reason to subject Dimension Cable or its Phoenix customers to the confusion and transaction costs that would result if we required Dimension Cable to retier.

V. ORDERING CLAUSES

21. Accordingly, IT IS ORDERED that Dimension Cable's package as it existed on December 13, 1993, may be treated as a new product tier under our *Going Forward Order*.

22. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[25] *Rate Order*, 8 FCC Rcd 5837, n.808 ("we do not think a cable operator can escape rate regulation simply by announcing that tiered services are available a la carte").

[26] *Second Reconsideration Order* ¶ 196.

[27] We are not precluding Dimension Cable from treating this package as a cable programming service tier, priced pursuant to our rules, or from putting the channels back into an existing tier.

[28] *Going Forward Order* ¶ ¶ 16-37.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

TKR Cable of Hamilton — LOI-93-31
Hamilton Township, New Jersey

Letter of Inquiry

MEMORANDUM OPINION AND ORDER

Adopted: November 23, 1994; Released: November 25, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. The Commission received a Form 329 Complaint on September 30, 1993, concerning the reasonableness of the rates charged for cable programming services by TKR Cable of Hamilton, Hamilton Township, New Jersey ("TKR"). In response to this complaint, the Commission issued Letter of Inquiry 93-31 ("LOI") to TKR on December 13, 1993.[1] The LOI asked TKR to provide information concerning its compliance with the Commission's rules governing evasion in the offering of packages which allegedly are not rate-regulated. TKR responded to our LOI on January 14, 1994.

II. BACKGROUND

2. In the Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act"), Congress created a regulatory scheme giving the Commission and local franchising authorities jurisdiction over the cable programming and equipment rates of non-competitive cable systems. The 1992 Cable Act provides that the rates of cable systems not subject to effective competition may be regulated by local franchising authorities, in the case of basic service, and by the Commission, in the case of cable programming services.[2] A stated policy of the 1992 Cable Act is to ensure that "consumer interests are protected in the receipt of cable service."[3]

3. The 1992 Cable Act requires cable operators to offer subscribers a basic tier that must contain at least all qualified local broadcast signals and, unless otherwise specified by the local franchising authority, public, educational, and governmental channels.[4] The Commission was charged by the 1992 Cable Act with creating regulations that ensure that the rates for the basic service tier are reasonable.[5] The 1992 Cable Act directs that "[s]uch regulations shall be designed to achieve the goal of protecting subscribers of any cable system that is not subject to effective competition from rates for the basic service tier that exceed the rates that would be charged for the basic service tier if such cable system were subject to effective competition."[6] Under the 1992 Cable Act, operators may offer other channels in a cable programming service tier or tiers.[7] The 1992 Cable Act orders the Commission to create regulations for the cable programming service tiers that allow it to identify individual cases of unreasonable rates.[8] The 1992 Cable Act thus protects consumers' interests in continuing to receive the basic service tier and cable programming service tiers at reasonable rates.

4. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[9] The 1992 Cable Act's legislative history states that the Commission should scrutinize offerings of non-traditional stand-alone services to "prevent repricing, retiering, or other alterations of rate structures" that could have the effect of evading the purposes of rate regulation.[10] This provision in the 1992 Cable Act is intended to give the Commission the authority to address changes in the cable industry's business practices that would thwart the intent of rate regulation.[11]

5. In the *Rate Order* the Commission defined evasion as "any practice or action which avoids the rate regulation provisions of the Cable Act or Commission rules contrary to the intent of the Act or its underlying policies."[12] We must scrutinize a particular operator's marketing or pricing practices to determine whether those practices have the effect of avoiding the requirements of our rate regulations, contrary to the intent of the 1992 Cable Act and our rules.

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[1] Letter from Roy J. Stewart, Chief, Mass Media Bureau, FCC, to TKR Cable of Hamilton, Hamilton Township, New Jersey, LOI-93-31 (December 13, 1993). Copies of the Letter of Inquiry and Response are available to the public in the FCC's Cable Reference Center, 2033 M Street, N.W., Room 207, Washington, D.C. We also note that there is a pending rate complaint proceeding involving TKR. Our decisions made herein will be made a part of that proceeding. Thus, for example, we will not order TKR to make refunds to subscribers in regard to TKR's purported "a la carte" restructuring. Obviously, however, we may order refunds if we find violations of other rules that should result in refunds.

[2] Communications Act of 1934 § 623 (a)(2), 47 U.S.C. § 543 0 (a)(2)(1992).

[3] Pub. L. No. 102-385 § 2 (b) (4) (1992); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. at 34 (1992).

[4] Communications Act of 1934 § 623 (b)(7)(A)(ii-iii), 47 U.S.C. § 543 (b)(7)(A)(ii-iii)(1992); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket 92-266, *Report and Order and Further Notice of Proposed Rulemaking,* 8 FCC Rcd 5631 ¶ 157-161 (1993) (*"Rate Order")* (franchising authorities may require operators to carry PEG channels on tiers other than basic).

[5] Communications Act of 1934 § 623 (b)(1), 47 U.S.C. § 543 (b)(1)(1992).

[6] *Id.*

[7] Communications Act of 1934 § 623(l)(2), 47 U.S.C. § 543(l)(2)(1992).

[8] Communications Act of 1934 § 623 (c)(1)(A), 47 U.S.C. § 543 (c)(1)(A)(1992). Identification of individual cases of unreasonable rates is achieved by a process in which the Commission assumes jurisdiction over systems where a complaint about a cable programming service tier rate is filed.

[9] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[10] H.R. Rep. No. 628, 102d Cong., 2d Sess. at 79 (1992).

[11] S. Rep. No. 92, 102d Cong., 2d Sess. at 77 (1992).

[12] *Rate Order* ¶ 451.

III. FACTS

6. Before September 1, 1993, TKR's services included a 22 channel basic tier, called Broadcast Basic, for $15.75 per month; a 2 channel cable programming service tier, called the Super Station Tier, for $1.00 per month; a 10 channel cable programming service tier, called Advantage, for $5.50 per month; and a 10 channel cable programming service tier, called Advantage Plus, for $1.00 per month. In order to receive either Advantage or Advantage Plus, subscribers were required to purchase both the Broadcast Basic tier and the Super Station Tier, and in order to receive Advantage Plus, subscribers were also required to purchase Advantage.

7. The following chart summarizes TKR's service tier offerings prior to September 1, 1993:

Offering	Channels	Price
1. Broadcast Basic	22	$15.75
2. Super Station Tier	2	$1.00
3. Advantage	10	$5.50
4. Advantage Plus	10	$1.00
Total	44	$23.25

8. Beginning August 31, 1993, the day before our rate regulations became effective, TKR restructured its service offerings. TKR's restructured service offerings included a 29 channel basic tier, called Broadcast Basic, for $16.09 per month and an 11 channel cable programming service tier, called Advantage, for $6.10 per month. TKR also began offering four channels in an a la carte package called Value Plus. The four channels were American Movie Classics, the Discovery Channel, Turner Network Television (TNT), and CNBC/Madison Square Garden Network (MSG) (shared channel). The Discovery Channel was originally in TKR's Advantage Plus tier and CNBC/MSG, TNT, and American Movie Classics were originally in TKR's Advantage tier.

9. TKR states that American Movie Classics, The Discovery Channel, TNT, and CNBC/MSG could be purchased individually for $0.85 per month. All four channels could be purchased as a package for $3.25 per month.

10. The following chart summarizes TKR's service tier options as of the date of its response to our LOI:[13]

Offering	Channels	Price
1. Broadcast Basic	29	$16.09
2. Advantage	11	$6.10
3. Value Plus	4	$3.25
Total	44	$25.44

11. TKR states that there is a one-time upgrade charge of $7.25 to receive either the Value Plus package or individual Value Plus channels. TKR further states that this charge was waived through October 31, 1993 for subscribers that purchased the Value Plus package. At the time of our LOI, there was an additional $2.00 "addressable converter activity fee" for subscribers to individual Value Plus channels who desired to add Value Plus channels, and a one-time $6.36 interdiction device installation charge and a $1.50 monthly charge for the device for subscribers who purchased individual Value Plus channels.

12. TKR argues, *inter alia*, that it began offering its services individually and through the Value Plus package in order to implement Congress' intent to maximize consumer choice. However, based on the record, very few consumers elected to exercise that choice. As of the date of its response, TKR states that two subscribers in the franchise area chose to subscribe to three or fewer of the individual Value Plus channels, while 26,158 subscribers in the franchise area took the entire Value Plus package.[14]

IV. DISCUSSION

13. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[15] An evasion, as defined by the Commission, is an act or practice that "avoids the rate regulation provisions of the [Cable] Act or our rules contrary to the intent of the Act or its underlying policies."[16] In the *Rate Order*, we stated that "retiering otherwise permitted under our rules will not be deemed an evasion."[17] First, we examine whether TKR's response to the LOI shows that its restructuring of its offerings had the effect of evading rate regulation for the channels that Congress intended to be rate-regulated.

14. TKR's restructuring effective August 31, 1993, involved its movement of one channel (The Discovery Channel) from its 10 channel Advantage Plus tier and three channels (American Movie Classics, TNT, and CNBC/MSG) from its 10 channel Advantage tier to create the four-channel package that it alleges is not rate-regulated. Thus, TKR removed channels from otherwise rate-regulated tiers to create a new package of channels. In so doing, TKR avoided application of our rate regulations which generally required cable operators to reduce rates by about 10 percent. That is, if TKR had not restructured on August 31, 1993, it would have been required to recalculate its rates in accordance with the *Rate Order* we released on May 3, 1993, which generally required cable operators to reduce their rates. Moreover, customers that were receiving the three Advantage tier channels and the one Advantage Plus tier channel at issue continued to receive them after the restructuring, and there appears to be no sufficient justification for TKR's restructuring other than to avoid rate regulation.

15. Other factors corroborate our view that TKR's restructuring may have had the effect of avoiding rate regulation. First, it offered this package on the eve of regulation. Second, it automatically subscribed its customers to the offerings that previously had been part of its cable programming service tiers. In light of these facts, it appears that TKR's restructuring of its offerings may have evaded rate regulation. We will not find an actual evasion occurred, however, if TKR's action complied with our a la carte policy that was in effect at the time of its

[13] This Order does not evaluate TKR's rates for its basic and cable programming service tiers. These rates are subject to review by the local franchising authority and the Commission in separate proceedings.

[14] TKR states that this data reflects subscribership as of December 21, 1993.

[15] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[16] *Rate Order* ¶ 451.

[17] *Id.* at ¶ 453.

restructuring. If the offering met our requirements for a permissible collective offering of a la carte channels, then TKR would not have evaded our rate regulations because it would not be required to reduce its price for the collective a la carte package.[18]

16. In our *Rate Order*, the Commission recognized that "a la carte packages" appear to be "cable programming services," but said that "interpreting the statute in such a literal fashion could disadvantage consumers by denying them discounts on packages of per-channel or per-program services and by limiting subscriber access to a greater quantity of premium programming."[19] Thus, we envisioned that cable operators, for the most part, would offer channels that previously had been offered a la carte in discounted packages, and concluded that it would be better for consumers if we construed the 1992 Cable Act to permit such discounting.[20] This is not the type of offering that TKR and others have provided their subscribers. Specifically, these operators did not offer a discounted package of channels that previously had been offered a la carte to subscribers, but instead removed channels from a tier that would be subject to our rate regulations.

17. Moreover, in the *Rate Order*, the Commission determined that such a la carte packages would be exempt from rate regulation, i.e., would be deemed not to fall within the definition of "cable programming service," if two conditions were met: (1) the price for the combined package must not exceed the sum of the individual charges for each component service; and (2) the cable operator must continue to provide the component parts of the package to subscribers separately in addition to the package. The Commission said that the second condition would be satisfied only when "the per channel offering provides consumers with a realistic service choice."[21]

18. Under the two-part test that we set forth in the *Rate Order*, it is clear, first, that the price for the combined package does not exceed the sum of the individual charges for the four services, because subscribers may purchase the four channels for $0.85 each or the four-channel package for $3.25. The second part of the test is whether the separate parts of the package constitute a "realistic service offering." The results of our review of TKR's submission reveal that far less than one percent of TKR's subscribers in the Hamilton Township franchise area chose to subscribe to individual Value Plus channels. Our test does not specify what number would indicate that an offering is "a realistic service offering." However, the fact that only two of TKR's subscribers in the franchise area chose to subscribe to individual Value Plus channels, together with the other factors present in this case,[22] tends to show, in this instance, that the per-channel offering does not constitute a realistic service offering.

19. Even if we were to apply the 15 interpretative guidelines set forth in our *Second Reconsideration Order*,[23] we still would not reach a clear answer to the question of what constitutes a realistic service offering. Although some factors support a finding that TKR's offering was not a permissible a la carte package, other factors point the other way. In particular, although a "significant percentage" of the channels offered in the a la carte package (100 percent) was removed from regulated tiers, the absolute number (four) was small.[24] Moreover, our test does not explain how the factors are to be weighed against each other. In these circumstances, we cannot say that it was clear to TKR that its restructuring was not a permissible a la carte package.

20. In our recently adopted *Going Forward Order*, we have reconsidered our rules relating to a la carte packages and concluded that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act. For that reason, the package at issue is subject to rate regulation and cannot continue to be treated as an unregulated package of channels. In reaching this conclusion in the *Going Forward Order*, we acknowledged that, as applied to many fact patterns, we did not provide a clear test in the *Rate Order* and the *Second Reconsideration Order* for determining whether an a la carte package was permissible. In adopting the 15 interpretive guidelines in the *Second Reconsideration Order* to supplement the *Rate Order's* two-prong test, we hoped to enable operators to better determine what collective offerings of a la carte channels would be considered a realistic service offering, and, hence, not an evasion of rate regulation.[25] Our experience to date, however, indicates that our efforts did not produce the intended result and that, instead, there has been confusion as to whether collective offerings of a la carte channels constituted an evasion of rate regulation. Indeed, we cannot say that it is clear that TKR's restructuring was not a permissible a la carte package.

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[18] In our *Going Forward Order*, we have reconsidered our regulatory treatment of collective offerings of a la carte channels. *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking*, MM Docket Nos. 92-266 and 93-215, FCC 94-286 (adopted November 10, 1994) *("Going Forward Order")*. Specifically, we have determined that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act and therefore will be subject to our general rate regulation rules. However, in order to determine whether TKR evaded rate regulation when it restructured its offering, we must evaluate its a la carte package under the rules that were in effect when it restructured.

[19] *Rate Order* ¶ *329*.

[20] *See, e.g., Rate Order* ¶ 453 n.1161 ("There is no evidence that operators would or, as a business matter, could shift programming previously offered as part of a tier to 'a la carte' status, *i.e.*, a per-channel or per-program offering, to avoid the rate regulation applicable to tiers").

[21] *Id.* at ¶ ¶ 327-28 & n.808. In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 92-266, *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking*, 9 FCC Rcd 4119 (1994) *("Second Reconsideration Order")*, the Commission affirmed its prior view. It said that "we continue to believe that the public interest will be served by generally permitting non-regulated treatment of collective offerings of 'a la carte' channels if the offering enhances consumer choice and does not constitute an evasion of rate regulation." *Id.* at ¶ 194. In this regard, we retained the two-part test contained in the *Rate Order* for determining when we would refrain from regulating "a la carte packages." In addition, the Commission set out 15 guidelines to enable operators to better determine what collective offerings of "a la carte" channels will be considered "realistic service offerings." *Id.* at ¶ 195.

[22] *See, e.g.*, ¶ ¶ 14-15, *supra*.

[23] *Second Reconsideration Order* at ¶ 196.

[24] *Id.*

[25] *See Going Forward Order* ¶ 40.

21. For that reason, we do not think that it would be equitable to subject TKR to refund liability. This result is distinguishable from the result we reached in *Adelphia Cable Partners, L.P.*,[26] in which we determined that we will require refunds if Adelphia's rate justification proceedings show that subscribers' rates were higher than our rules permitted. In that case, the cable operator announced that it would offer all the channels previously offered on a cable programming service tier on an individual basis or as a collective offering of a la carte channels. In so doing, Adelphia removed an entire service tier from rate regulation. In contrast, TKR attempted to treat only four channels as an unregulated collective offering of a la carte channels. Moreover, while we have indicated above that our rules for determining whether collective offerings of a la carte channels constitute an evasion were in many instances difficult to apply, we do not believe that our a la carte rules are unclear as applied to the fact pattern in the *Adelphia* case. In the *Rate Order,* we stated that a cable operator could not escape rate regulation simply by calling what otherwise would be a rate regulated tier an a la carte package.[27] We reiterated this admonition in the *Second Reconsideration Order* when we warned against eliminating "an entire regulated tier" and "turning it into an a la carte package."[28]

22. We will not require TKR to restructure its tiers so as to return the channels offered in the a la carte package to the basic or cable programming service tiers,[29] instead, on a prospective basis, therefore, we will consider TKR's collective offering of a la carte channels a new product tier[30] even though it would not qualify as a new product tier under our recently announced *Going Forward Order* because one of the conditions for a new product tier is that channels may not be removed from a basic service tier or a cable programming service tier. In light of the prior confusion over what constituted a permissible a la carte offering, and because TKR's four-channel tier, unlike Adelphia's offering, did not constitute a clear evasion of our rate rules, we see no good reason to subject TKR or its Hamilton Township customers to the confusion and transaction costs that would result if we required TKR to retier.

V. ORDERING CLAUSES

23. Accordingly, IT IS ORDERED that TKR's package as it existed on January 14, 1994, may be treated as a new product tier under our *Going Forward Order.*

24. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

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[26] *Adelphia Cable Partners, L.P.*, South Dade County, Florida, LOI-93-42, FCC 94-1277 (released November 18, 1994).

[27] *Rate Order,* 8 FCC Rcd 5837, n.808 ("we do not think a cable operator can escape rate regulation simply by announcing that tiered services are available a la carte").

[28] *Second Reconsideration Order* ¶ 196.

[29] We are not precluding TKR from treating this package as a cable programming service tier, priced pursuant to our rules, or from putting the channels back into an existing tier.

[30] *Going Forward Order* ¶ ¶ 16-37.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

TKR Cable of Greater Louisville, Kentucky — LOI-93-46

Letter of Inquiry

MEMORANDUM OPINION AND ORDER

Adopted: November 23, 1994; Released: November 25, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. In a Form 329 Complaint filed with the Commission on October 29, 1993, the City of Louisville, Kentucky alleged violations by TKR Cable of Greater Louisville ("TKR") of Commission regulations governing the provision of cable television service. In response to this complaint, the Commission issued Letter of Inquiry 93-46 ("LOI") to TKR on December 13, 1993.[1] The LOI asked TKR to provide information concerning its compliance with the Commission's rules governing evasion in the offering of packages which allegedly are not rate-regulated. TKR responded to our LOI on January 14, 1994.

II. BACKGROUND

2. In the Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act"), Congress created a regulatory scheme giving the Commission and local franchising authorities jurisdiction over the cable programming and equipment rates of non-competitive cable systems. The 1992 Cable Act provides that the rates of cable systems not subject to effective competition may be regulated by local franchising authorities, in the case of basic service, and by the Commission, in the case of cable programming services.[2] A stated policy of the 1992 Cable Act is to ensure that "consumer interests are protected in the receipt of cable service."[3]

3. The 1992 Cable Act requires cable operators to offer subscribers a basic tier that must contain at least all qualified local broadcast signals and, unless otherwise specified by the local franchising authority, public, educational, and governmental channels.[4] The Commission was charged by the 1992 Cable Act with creating regulations that ensure that the rates for the basic service tier are reasonable.[5] The 1992 Cable Act directs that "[s]uch regulations shall be designed to achieve the goal of protecting subscribers of any cable system that is not subject to effective competition from rates for the basic service tier that exceed the rates that would be charged for the basic service tier if such cable system were subject to effective competition."[6] Under the 1992 Cable Act, operators may offer other channels in a cable programming service tier or tiers.[7] The 1992 Cable Act orders the Commission to create regulations for the cable programming service tiers that allow it to identify individual cases of unreasonable rates.[8] The 1992 Cable Act thus protects consumers' interests in continuing to receive the basic service tier and cable programming service tiers at reasonable rates.

4. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[9] The 1992 Cable Act's legislative history states that the Commission should scrutinize offerings of non-traditional stand-alone services to "prevent repricing, retiering, or other alterations of rate structures" that could have the effect of evading the purposes of rate regulation.[10] This provision in the 1992 Cable Act is intended to give the Commission the authority to address changes in the cable industry's business practices that would thwart the intent of rate regulation.[11]

5. In the *Rate Order* the Commission defined evasion as "any practice or action which avoids the rate regulation provisions of the Cable Act or Commission rules contrary to the intent of the Act or its underlying policies."[12] We must scrutinize a particular operator's marketing or pricing practices to determine whether those practices have the effect of avoiding the requirements of our rate regulations, contrary to the intent of the 1992 Cable Act and our rules.

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[1] Letter from Roy J. Stewart, Chief, Mass Media Bureau, FCC, to TKR Cable of Greater Louisville, Kentucky, LOI-93-46 (December 13, 1993). Copies of the Letter of Inquiry and Response are available to the public in the FCC's Cable Reference Center, 2033 M Street, N.W., Room 207, Washington, D.C. We also note that there is a pending rate complaint proceeding involving TKR. Our decisions made herein will be made a part of that proceeding. Thus, for example, we will not order TKR to make refunds to subscribers in regard to TKR's purported "a la carte" restructuring. Obviously, however, we may order refunds if we find violations of other rules that should result in refunds.

[2] Communications Act of 1934 § 623 (a)(2), 47 U.S.C. § 543 (a)(2)(1992).

[3] Pub. L. No. 102-385 § 2 (b) (4) (1992); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. at 34 (1992).

[4] Communications Act of 1934 § 623 (b)(7)(A)(ii-iii), 47 U.S.C. § 543 (b)(7)(A)(ii-iii)(1992); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket 92-266, *Report and Order and Further Notice of Proposed Rulemaking,* 8 FCC Rcd 5631 ¶ ¶ 157-161 (1993) (*"Rate Order"*) (franchising authorities may require operators to carry PEG channels on tiers other than basic).

[5] Communications Act of 1934 § 623 (b)(1), 47 U.S.C. § 543 (b)(1)(1992).

[6] *Id.*

[7] Communications Act of 1934 § 623(l)(2), 47 U.S.C. § 543(l)(2)(1992).

[8] Communications Act of 1934 § 623 (c)(1)(A), 47 U.S.C. § 543 (c)(1)(A)(1992). Identification of individual cases of unreasonable rates is achieved by a process in which the Commission assumes jurisdiction over systems where a complaint about a cable programming service tier rate is filed.

[9] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[10] H.R. Rep. No. 628, 102d Cong., 2d Sess. at 79 (1992).

[11] S. Rep. No. 92, 102d Cong., 2d Sess. at 77 (1992).

[12] *Rate Order* ¶ 451.

III. FACTS

6. Before September 1, 1993, TKR's services included a 15 channel basic tier for $8.77 per month, a 19 channel cable programming service tier, called the Classic tier, for $11.11 per month, and an additional 2 channel programming service tier, called the Superstations tier, for $1.17 per month.[13] In order to receive the Classic tier, subscribers were required to purchase both the basic tier and the Superstations tier.

7. The following chart summarizes TKR's service tier offerings prior to September 1, 1993:

Offering	Channels	Price
1. Basic tier	15	$8.77
2. Classic tier	19	$11.11
3. Superstations tier	2	$1.17
Total	36	$21.05

8. Beginning August 31, 1993, the day before our rate regulations became effective, TKR restructured its service offerings. TKR's restructured service offerings included a 17 channel basic tier for $10.81 per month and a 15 channel cable programming service tier, called the Classic tier, for $9.54 per month. TKR also began offering four channels in an a la carte package called Plus 4. The four channels were American Movie Classics, The Disney Channel, WTBS, and WGN. WTBS and WGN were originally in TKR's Superstations tier and American Movie Classics and The Disney Channel were originally in TKR's Classic tier.

9. TKR states that American Movie Classics, The Disney Channel, WTBS, and WGN could be purchased individually for $0.50 per month. All four channels could be purchased as a package for $1.85 per month.

10. The following chart summarizes TKR's service tier options as of the date of its response to our LOI:[14]

Offering	Channels	Price
1. Basic tier	17	$10.81
2. Classic tier	15	$9.54
3. Plus 4	4	$1.85
Total	36	$22.20

11. TKR states that American Movie Classics, The Disney Channel, WTBS, and WGN can be purchased either individually or collectively without purchasing any other level of service except basic service. TKR explains, however, that an interdiction device is needed if a subscriber wishes to purchase any of the channels individually. At the time of our LOI, there was a one-time installation charge of $3.46 and a monthly charge of $1.00 for the interdiction device. TKR states that installation charges for the interdiction device were waived from mid-August 1993 through September 30, 1993.

12. TKR argues, *inter alia*, that it began offering its services individually and through the Plus 4 package in order to implement Congress' intent to maximize consumer choice. However, based on the record, very few consumers elected to exercise that choice. As of the date of its response, TKR states that four subscribers in the franchise area chose to subscribe to three or fewer of the Plus 4 a la carte channels, while 62,364 subscribers in the franchise area took the Plus 4 package.[15]

IV. DISCUSSION

13. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[16] An evasion, as defined by the Commission, is an act or practice that "avoids the rate regulation provisions of the [Cable] Act or our rules contrary to the intent of the Act or its underlying policies."[17] In the *Rate Order*, we stated that "retiering otherwise permitted under our rules will not be deemed an evasion."[18] First, we examine whether TKR's response to the LOI shows that its restructuring of its offerings had the effect of evading rate regulation for the channels that Congress intended to be rate-regulated.

14. TKR's restructuring effective August 31, 1993, involved its movement of two channels (American Movie Classics and The Disney Channel) from its 19 channel Classic tier and two channels (WTBS and WGN) from its two channel Superstations tier to create the four-channel package that it alleges is not rate-regulated. Thus, TKR removed channels from otherwise rate-regulated tiers to create a new package of channels. In so doing, TKR avoided application of our rate regulations which generally required cable operators to reduce rates by about 10 percent. That is, if TKR had not restructured on August 31, 1993, it would have been required to recalculate its rates in accordance with the *Rate Order* we released on May 3, 1993, which generally required cable operators to reduce their rates. Moreover, customers that were receiving the two Superstations tier channels and the two Classic tier channels at issue continued to receive them after the restructuring, and there appears to be no sufficient justification for TKR's restructuring other than to avoid rate regulation.

15. Other factors corroborate our view that TKR's restructuring may have had the effect of avoiding rate regulation. First, it offered this package on the eve of regulation. Second, it automatically subscribed its customers to the offerings that previously had been part of its basic and cable programming service tiers. In light of these facts, it appears that TKR's restructuring of its offerings may have evaded rate regulation. We will not find an actual evasion occurred, however, if TKR's action complied with our a la carte policy that was in effect at the time of its restructuring. If the offering met our requirements for a permissible collective offering of a la carte channels, then

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[13] These rates were in effect from June 21, 1993 through August 30, 1993.

[14] This Order does not evaluate TKR's rates for its basic and cable programming service tiers. These rates are subject to review by the local franchising authority and the Commission in separate proceedings.

[15] TKR states that this data reflects subscribership as of December 24, 1993.

[16] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[17] *Rate Order* ¶ 451.

[18] *Id.* at ¶ 453.

TKR would not have evaded our rate regulations because it would not be required to reduce its price for the collective a la carte package. [19]

16. In our *Rate Order,* the Commission recognized that "a la carte packages" appear to be "cable programming services," but said that "interpreting the statute in such a literal fashion could disadvantage consumers by denying them discounts on packages of per-channel or per-program services and by limiting subscriber access to a greater quantity of premium programming.[20] Thus, we envisioned that cable operators, for the most part, would offer channels that previously had been offered a la carte in discounted packages, and concluded that it would be better for consumers if we construed the 1992 Cable Act to permit such discounting.[21] This is not the type of offering that TKR andpothers have provided their subscribers. Specifically, these operators did not offer a discounted package of channels that previously had been offered a la carte to subscribers, but instead removed channels from a tier that would be subject to our rate regulations.

17. Moreover, in the *Rate Order,* the Commission determined that such a la carte packages would be exempt from rate regulation, i.e., would be deemed not to fall within the definition of "cable programming service," if two conditions were met: (1) the price for the combined package must not exceed the sum of the individual charges for each component service; and (2) the cable operator must continue to provide the component parts of the package to subscribers separately in addition to the package. The Commission said that the second condition would be satisfied only when "the per channel offering provides consumers with a realistic service choice."[22]

18. Under the two-part test that we set forth in the *Rate Order,* it is clear, first, that the price for the combined package does not exceed the sum of the individual charges for the four services, because subscribers may purchase the four channels for $0.50 each or the four-channel package for $1.85. The second part of the test is whether the separate parts of the package constitute a "realistic service offering." The results of our review of TKR's submission reveal that far less than one percent of TKR's subscribers in the Louisville franchise area chose to subscribe to individual Plus 4 channels. Our test does not specify what number would indicate that an offering is "a realistic service offering." However, the fact that only four of TKR's subscribers in the franchise area chose to subscribe to individual Plus 4 channels, together with the other factors present in this case,[23] tends to show, in this instance, that the per-channel offering does not constitute a realistic service offering.

19. Even if we were to apply the 15 interpretative guidelines set forth in our *Second Reconsideration Order,*[24] we still would not reach a clear answer to the question of what constitutes a realistic service offering. Although some factors support a finding that TKR's offering was not a permissible a la carte package, other factors point the other way. In particular, although a "significant percentage" of the channels offered in the a la carte package (100 percent) was removed from regulated tiers, the absolute number (four) was small.[25] Moreover, our test does not explain how the factors are to be weighed against each other. In these circumstances, we cannot say that it was clear to TKR that its restructuring was not a permissible a la carte package.

20. In our recently adopted *Going Forward Order,* we have reconsidered our rules relating to a la carte packages and concluded that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act. For that reason, the package at issue is subject to rate regulation and cannot continue to be treated as an unregulated package of channels. In reaching this conclusion in the *Going Forward Order,* we acknowledged that, as applied to many fact patterns, we did not provide a clear test in the *Rate Order* and the *Second Reconsideration Order* for determining whether an a la carte package was permissible. In adopting the 15 interpretive guidelines in the *Second Reconsideration Order* to supplement the *Rate Order's* two-prong test, we hoped to enable operators to better determine what collective offerings of a la carte channels would be considered a realistic service offering, and, hence, not an evasion of rate regulation.[26] Our experience to date, however, indicates that our efforts did not produce the intended result and that, instead, there has been confusion as to whether collective offerings of a la carte channels constituted an evasion of rate regulation. Indeed, we cannot say that it is clear that TKR's restructuring was not a permissible a la carte package.

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[19] In our *Going Forward Order,* we have reconsidered our regulatory treatment of collective offerings of a la carte channels. *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking,* MM Docket Nos. 92-266 and 93-215, FCC 94-286 (adopted November 10, 1994) *("Going Forward Order").* Specifically, we have determined that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act and therefore will be subject to our general rate regulation rules. However, in order to determine whether TKR evaded rate regulation when it restructured its offering, we must evaluate its a la carte package under the rules that were in effect when it restructured.

[20] *Rate Order* ¶ *329.*

[21] *See, e.g., Rate Order* ¶ 453 n.1161 ("There is no evidence that operators would or, as a business matter, could shift programming previously offered as part of a tier to 'a la carte' status, *i.e.,* a per-channel or per-program offering, to avoid the rate regulation applicable to tiers").

[22] *Id.* at ¶ ¶ 327-28 & n.808. In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-266, *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking,* 9 FCC Rcd 4119 (1994) *("Second Reconsideration Order"),* the Commission affirmed its prior view. It said that "we continue to believe that the public interest will be served by generally permitting non-regulated treatment of collective offerings of §a la carte§ channels if the offering enhances consumer choice and does not constitute an 8evasion of rate regulation." *Id.* at ¶ 1

94. In this regard, we retained the two-part test contained in the *Rate Order* for determining when we would refrain from regulating "a la carte packages." In addition, the Commission set out 15 guidelines to enable operators to better determine what collective offerings of "a la carte" channels will be considered "realistic service offerings." *Id.* at ¶ 195.

[23] *See, e.g.,* ¶ ¶ 14-15, *supra.*

[24] *Second Reconsideration Order* at ¶ 196.

[25] *Id.*

[26] *See Going Forward Order* ¶ 40.

21. For that reason, we do not think that it would be equitable to subject TKR to refund liability. This result is distinguishable from the result we reached in *Adelphia Cable Partners, L.P.*,[27] in which we determined that we will require refunds if Adelphia's rate justification proceedings show that subscribers' rates were higher than our rules permitted. In that case, the cable operator announced that it would offer all the channels previously offered on a cable programming service tier on an individual basis or as a collective offering of a la carte channels. In so doing, Adelphia removed an entire service tier from rate regulation. In contrast, TKR attempted to treat only four channels as an unregulated collective offering of a la carte channels. Moreover, while we have indicated above that our rules for determining whether collective offerings of a la carte channels constitute an evasion were in many instances difficult to apply, we do not believe that our a la carte rules are unclear as applied to the fact pattern in the *Adelphia* case. In the *Rate Order*, we stated that a cable operator could not escape rate regulation simply by calling what otherwise would be a rate regulated tier an a la carte package.[28] We reiterated this admonition in the *Second Reconsideration Order* when we warned against eliminating "an entire regulated tier" and "turning it into an a la carte package."[29]

22. We will not require TKR to restructure its tiers so as to return the channels offered in the a la carte package to the basic or cable programming service tiers,[30] instead, on a prospective basis, therefore, we will consider TKR's collective offering of a la carte channels a new product tier[31] even though it would not qualify as a new product tier under our recently announced *Going Forward Order* because one of the conditions for a new product tier is that channels may not be removed from a basic service tier or a cable programming service tier. In light of the prior confusion over what constituted a permissible a la carte offering, and because TKR's four-channel tier, unlike Adelphia's offering, did not constitute a clear evasion of our rate rules, we see no good reason to subject TKR or its Louisville customers to the confusion and transaction costs that would result if we required TKR to retier.

V. ORDERING CLAUSES

23. Accordingly, IT IS ORDERED that TKR's package as it existed on January 14, 1994, may be treated as a new product tier under our *Going Forward Order*.

24. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

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[27] *Adelphia Cable Partners, L.P.*, South Dade County, Florida, LOI-93-42, FCC 94-1277 (released November 18, 1994).

[28] *Rate Order*, 8 FCC Rcd 5837, n.808 ("we do not think a cable operator can escape rate regulation simply by announcing that tiered services are available a la carte").

[29] *Second Reconsideration Order* ¶ 196.

[30] We are not precluding TKR from treating this package as a cable programming service tier, priced pursuant to our rules, or from putting the channels back into an existing tier.

[31] *Going Forward Order* ¶ ¶ 16-37.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Paragon Cable LOI-93-25
Irving, TX

Letter of Inquiry

MEMORANDUM OPINION AND ORDER

Adopted: November 23, 1994; Released: November 25, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. In a letter received by the Commission, dated September, 28, 1994, the City of Irving alleged violations by Paragon Cable ("Paragon") of Commission regulations governing the provision of cable television service. In response to this complaint, the Commission issued Letter of Inquiry 93-25 ("LOI") to Paragon on December 13, 1993.[1] The LOI asked Paragon to provide information concerning, among other issues, its compliance with the Commission's rules governing evasion in the offering of packages which allegedly are not rate-regulated.[2] Paragon responded to our LOI on January 11, 1994.

II. BACKGROUND

2. In the Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act"), Congress created a regulatory scheme giving the Commission and local franchising authorities jurisdiction over the cable programming and equipment rates of non-competitive cable systems. The 1992 Cable Act provides that the rates of cable systems not subject to effective competition may be regulated by local franchising authorities, in the case of basic service, and by the Commission, in the case of cable programming services.[3] A stated policy of the 1992 Cable Act is to ensure that "consumer interests are protected in the receipt of cable service."[4]

3. The 1992 Cable Act requires cable operators to offer subscribers a basic tier that must contain at least all qualified local broadcast signals and, unless otherwise specified by the local franchising authority, public, educational, and governmental channels.[5] The Commission was charged by the 1992 Cable Act with creating regulations that ensure that the rates for the basic service tier are reasonable.[6] The 1992 Cable Act directs that "[s]uch regulations shall be designed to achieve the goal of protecting subscribers of any cable system that is not subject to effective competition from rates for the basic service tier that exceed the rates that would be charged for the basic service tier if such cable system were subject to effective competition."[7] Under the 1992 Cable Act, operators may offer other channels in a cable programming service tier or tiers.[8] The 1992 Cable Act orders the Commission to create regulations for the cable programming service tiers that allow it to identify individual cases of unreasonable rates.[9] The 1992 Cable Act thus protects consumers' interests in continuing to receive the basic service tier and cable programming service tiers at reasonable rates.

4. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[10] The 1992 Cable Act's legislative history states that the Commission should scrutinize offerings of non-traditional stand-alone services to "prevent repricing, retiering, or other alterations of rate

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[1] Letter from Roy J. Stewart, Chief, Mass Media Bureau, FCC, to Walter Nesbit, Vice President of Operations, Paragon Cable, LOI-93-25 (December 13, 1993). Copies of the Letter of Inquiry and Response are available to the public in the FCC's Cable Reference Center, 2033 M Street, N.W., Room 207, Washington, D.C. We also note that there is a pending rate complaint proceeding involving Paragon. Our decisions made herein will be made a part of that proceeding. Thus, for example, we will not order Paragon to make refunds to subscribers in regard to Paragon's purported "a la carte" restructuring. Obviously, however, we may order refunds if we find violations of other rules that should result in refunds.

[2] The LOI also requested information concerning elimination of senior discounts, items denoted as FCC adjustments, negative option billing and compliance with regulations governing the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket 92-266, *Order*, 8 FCC Rcd 2921 (1993) (*"Rate Freeze Order"), clarified*, 8 FCC Rcd 2917, 58 FR 21929 (April 26, 1993); *extended*, FCC 93-304 (released June 15, 1993), 58 FR 33560 (June 18, 1993), *Erratum*, 8 FCC Rcd 4511 (1993); *extended*, FCC 93-494 (released November 10, 1993), 58 FR 60141 (November 15, 1993); *extended*, 9 FCC Rcd 1299, 59 FR 6901 (February 14, 1994). This Order addresses only the regulatory status of the package. Other issues in the LOI will be dealt with subsequently.

[3] Communications Act of 1934 § 623 (a)(2), 47 U.S.C. § 543 8(a)(2)(1992).

[4] Pub. L. No. 102-385 § 2 (b) (4) (1992); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. at 34 (1992).

[5] Communications Act of 1934 § 623 (b)(7)(A)(ii-iii), 47 U.S.C. § 543 (b)(7)(A)(ii-iii)(1992); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket 92-266, *Report and Order and Further Notice of Proposed Rulemaking*, 8 FCC Rcd 5631 ¶ ¶ 157-161 (1993) (*"Rate Order"*) (franchising authorities may require operators to carry PEG channels on tiers other than basic).

[6] Communications Act of 1934 § 623 (b)(1), 47 U.S.C. § 543 (b)(1)(1992).

[7] *Id.*

[8] Communications Act of 1934 § 623(l)(2), 47 U.S.C. § 543(l)(2)(1992).

[9] Communications Act of 1934 § 623 (c)(1)(A), 47 U.S.C. § 543 (c)(1)(A)(1992). Identification of individual cases of unreasonable rates is achieved by a process in which the Commission assumes jurisdiction over systems where a complaint about a cable programming service tier rate is filed.t

[10] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

structures" that could have the effect of evading the purposes of rate regulation.[11] This provision in the 1992 Cable Act is intended to give the Commission the authority to address changes in the cable industry's business practices that would thwart the intent of rate regulation.[12]

5. In the *Rate Order* the Commission defined evasion as "any practice or action which avoids the rate regulation provisions of the Cable Act or Commission rules contrary to the intent of the Act or its underlying policies."[13] We must scrutinize a particular operator's marketing or pricing practices to determine whether those practices have the effect of avoiding the requirements of our rate regulations, contrary to the intent of the 1992 Cable Act and our rules.

III. FACTS

6. Before September 1, 1993, Paragon's services included a 22 channel basic tier for $9.95 per month and a 25 channel cable programming service tier, called the standard tier, for $13.68 per month:

Offering	Channels	Price
1. Basic	22	$ 9.95
2. Standard	25	$13.68
TOTAL	47	$23.63

7. On September 1, 1993, the date our rate regulations became effective, Paragon states that two channels, WTBS and WGN, were moved from the basic tier and offered to its subscribers on an individual or package basis.[14] Paragon states that these channels could be purchased individually for $1.00 each or as a package for $1.50. Paragon also changed its basic tier rate to $9.70 and its standard tier rate to $11.47. The following chart summarizes Paragon's service tier options as of the date of its response to our LOI:[15]

Offering	Channels	Price
1. Basic	22	$ 9.70
2. Standard	26	$11.47
3. Package	2	$1.50 or $1.00 per channel
TOTAL	50	$22.67 (if purchased package)

Paragon's restructuring allowed customers to receive 50 channels at a total price of $22.67 per month. Paragon did not indicate what if any equipment was necessary to subscribe to the two individual channels; however, it indicated that converter charges of $1.31 for non-addressable converters and $1.64 for addressable converters were introduced at the same time as the package was.

8. Paragon argues, *inter alia,* that it began offering its services individually and through its package in order to implement Congress' intent to maximize consumer choice. However, based on this record, very few consumers elected to exercise that choice. Paragon's response provides a breakdown of its subscribers who chose the package of individual channels. Of 31,429 total subscribers, 25,204 or 80 percent, subscribe to the a la carte package; 32 subscribers, or one percent subscribe to one or more of the individual a la carte channels.

IV. DISCUSSION

9. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[16] An evasion, as defined by the Commission, is an act or practice that "avoids the rate regulation provisions of the [Cable] Act or our rules contrary to the intent of the Act or its underlying policies."[17] In the *Rate Order,* we stated that "retiering otherwise permitted under our rules will not be deemed an evasion."[18] First, we examine whether Paragon's response to the LOI shows that its restructuring of its offerings had the effect of evading rate regulation for the channels that Congress intended to be rate-regulated.

10. Paragon's restructuring effective September 1, 1993, involved its movement of 2 channels (WTBS and WGN) from its basic tier to create the two-channel package that it alleges is not rate-regulated. Thus, Paragon removed channels from an otherwise rate-regulated tier to create a new package of channels. In so doing, Paragon avoided application of our rate regulations which generally required cable operators to reduce rates by about 10 percent. That is, if Paragon had not restructured on prior to September 1, 1993, it would have been required to recalculate its rates in accordance with the *Rate Order* we released on May 3, 1993, which generally required cable operators to reduce their rates. Moreover, customers that were receiving the basic tier continued to receive the two channels at issue after the restructuring. There appears, therefore, to be no sufficient justification for Paragon's restructuring other than to avoid rate regulation.

11. Other factors corroborate our view that Paragon's restructuring may have had the effect of avoiding rate regulation. First, it offered this package on the eve of regulation. Second, it automatically subscribed its customers to the offerings that previously had been part of its basic tier. In light of these facts, it appears that Paragon's restructuring of its offerings may have evaded rate regulation. We will not find an actual evasion occurred, however, if Paragon's action complied with our a la carte policy that was in effect at the time of its restructuring. If the offering met the Commission's requirements for a permissible collective offering of a la carte channels, then Paragon

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[11] H.R. Rep. No. 628, 102d Cong., 2d Sess. at 79 (1992).
[12] S. Rep. No. 92, 102d Cong., 2d Sess. at 77 (1992).
[13] *Rate Order* ¶ 451.
[14] Paragon explains that between April 8, 1993 and September 1, 1993, it made numerous changes in its programming, including adding, dropping and moving certain channels. As a result of these changes, the number of channels on the standard tier increased from 25 to 26 between April and September, 1993 and the number of channels on the basic tier remained 22, despite the removal of the two channels at issue.
[15] This order does not evaluate Paragon's rates for its basic and cable programming service tiers. These rates are subject to review by the local franchising authority and the Commission in separate proceedings.
[16] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).
[17] *Rate Order* ¶ 451.
[18] *Id.* at ¶ 453.

would not have evaded our rate regulations because it would not be required to reduce its price for the collective a la carte package.[19]

12. In our *Rate Order,* the Commission recognized that "a la carte packages" appear to be "cable programming services," but said that "interpreting the statute in such a literal fashion could disadvantage consumers by denying them discounts on packages of per-channel or per-program services and by limiting subscriber access to a greater quantity of premium programming."[20] Thus, we envisioned that cable operators, for the most part, would offer channels that previously had been offered a la carte in discounted packages, and concluded that it would be better for consumers if we construed the 1992 Cable Act to permit such discounting.[21] This is not the type of offering that Paragon and others have provided their subscribers. Specifically, these operators did not offer a discounted package of channels that previously had been offered a la carte to subscribers, but instead removed channels from a tier that would be subject to our rate regulations.

13. Moreover, in the *Rate Order,* the Commission determined that a la carte packages would be exempt from rate regulation, i.e., would be deemed not to fall within the definition of "cable programming service," if two conditions were met: (1) the price for the combined package must not exceed the sum of the individual charges for each component service; and (2) the cable operator must continue to provide the component parts of the package to subscribers separately in addition to the package. The Commission said that the second condition would be satisfied only when "the per channel offering provides consumers with a realistic service choice."[22]

14. Under the two-part test that we set forth in the *Rate Order,* it is clear, first, that the price for the combined package does not exceed the sum of the individual charges for the two services, because subscribers may purchase each channel for $1.00 or the two-channel package for $1.50. The second part of the test is whether the separate parts of the package constitute a "realistic service offering." The results of our review of Paragon's submission reveal that approximately 99 percent of the subscribers in Irving did not choose to subscribe to individual a la carte channels. Although only 6,225 of Paragon's 31,429 subscribers chose not to purchase the a la carte package, our test does not specify what percentage would indicate that an offering is "a realistic service offering." However, this fact, together with the other factors present in this case,[23] tends to show that the per-channel offering, in this instance, does not constitute a realistic service offering.

15. Even if we were to apply the 15 interpretative guidelines set forth in our *Second Reconsideration Order,*[24] we still would not reach a clear answer to the question of what constitutes a realistic service offering. Although some factors support a finding that Paragon's offering was not a permissible a la carte package, other factors point the other way. In particular, although a "significant percentage" of the channels offered in the a la carte package (100 percent) was removed from a regulated tier, the absolute number (two) was small.[25] Moreover, our test does not explain how the factors are to be weighed against each other. In these circumstances, we cannot say that it was clear to Paragon that its restructuring was not a permissible a la carte package.

16. In our recently adopted *Going Forward Order,* we have reconsidered our rules relating to a la carte packages and concluded that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act. For that reason, the package at issue is subject to rate regulation and cannot continue to be treated as an unregulated package of channels. In reaching this conclusion in the *Going Forward Order,* we acknowledged that, as applied to many fact patterns, we did not provide a clear test in the *Rate Order* and the *Second Reconsideration Order* for determining whether an a la carte package was permissible. In adopting the 15 interpretive guidelines in the *Second Reconsideration Order* to supplement the *Rate Order*'s two-prong test, we hoped to enable operators to better determine what collective offerings of a la carte channels would be considered an evasion of rate regulation.[26] Our experience to date, however, indicates that our efforts did not produce the intended result and that, instead, there has been confusion as to whether collective offerings of a la carte channels constituted an evasion of rate regulation. Indeed, we cannot say that it is clear that Paragon's restructuring was not a permissible a la carte package.

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[19] In our *Going Forward Order,* we have reconsidered our regulatory treatment of collective offerings of a la carte channels. *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking,* MM Docket Nos. 92-266 and 93-215, FCC 94-286 (adopted November 10, 1994) *("Going Forward Order").* Specifically, we have determined that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act and therefore will be subject to our general rate regulation rules. However, in order to determine whether Paragon evaded rate regulation when it restructured its offering, we must evaluate its a la carte package under the rules that were in effect when it restructured.

[20] *Rate Order* ¶ 329.

[21] *See, e.g., Rate Order* at ¶ 453 n.1161 ("There is no evidence that operators would or, as a business matter, could shift programming previously offered as part of a tier to 'a la carte' status, *i.e.,* a per-channel or per-program offering, to avoid the rate regulation applicable to tiers").

[22] *Id.* at ¶ ¶ 327-28 & n.808. In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-266, *Second Order on Reconsideration, Fourth Report & Order, and Fifth Notice of Proposed Rulemaking,* 9 FCC Rcd 4119 (1994) (*"Second Reconsideration Order"*), the Commission affirmed its prior view. It said that "we continue to believe that the public interest will be served by generally permitting non-regulated treatment of collective offerings of 'a la carte' channels if the offering enhances consumer choice and does not constitute an evasion of rate regulation." *Id.* at ¶ 194. In this regard, we retained the two-part test contained in the *Rate Order* for determining when we would refrain from regulating "a la carte packages." In addition, the Commission set out 15 interpretive guidelines to enable operators to better determine what collective offerings of "a la carte" channels will be considered "realistic service offerings." *Id.* at ¶ 195.

[23] *See* ¶ ¶ 10-11, *supra.*

[24] *Second Reconsideration Order* ¶ 196.

[25] *Id.*

[26] *See Going Forward Order* ¶ 40.

17. For that reason, we do not think that it would be equitable to subject Paragon to refund liability. This result is distinguishable from the result we reached in *Adelphia Cable Partners, L.P.*,[27] in which we determined that we will require refunds if Adelphia's rate justification proceedings show that subscribers' rates were higher than our rules permitted. In that case, the cable operator announced that it would offer all the channels previously offered on a cable programming service tier on an individual basis or as a collective offering of a la carte channels. In so doing, Adelphia removed an entire service tier from rate regulation. In contrast, Paragon attempted to treat only two channels as an unregulated collective offering of a la carte channels. Moreover, while we have indicated above that our rules for determining whether collective offerings of a la carte channels constitute an evasion were, in many instances, unclear, we do not believe that our a la carte rules are unclear as applied to the fact pattern in the *Adelphia* case. In the *Rate Order*, we stated that a cable operator could not escape rate regulation simply by calling what otherwise would be a rate regulated tier an a la carte package.[28] We reiterated this admonition in the *Second Reconsideration Order* when we warned against eliminating "an entire regulated tier" and "turning it into an a la carte package."[29]

18. We will not require Paragon to restructure its tiers so as to return the channels offered in the a la carte package to the basic tier,[30] instead, on a prospective basis, we will consider Paragon's collective offering of a la carte channels a new product tier[31] even though it would not qualify as a new product tier under our recently announced *Going Forward Order* because one of the conditions for a new product tier is that channels may not be removed from a basic service tier or a cable programming service tier. In light of the prior confusion over what constituted a permissible a la carte offering, and because Paragon's two-channel tier, unlike Adelphia's offering, did not constitute a clear evasion of our rate rules, we see no good reason to subject Paragon or its Irving customers to the confusion and transaction costs that would result if we required Paragon to retier.

V. ORDERING CLAUSES

19. Accordingly, IT IS ORDERED that Paragon's package as it existed on December 13, 1993, may be treated as a new product tier under our *Going Forward Order*.

20. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

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[27] *Adelphia Cable Partners, L.P.*, South Dade County, Florida, LOI-93-42, FCC 94-1277 (released November 18, 1994).

[28] *Rate Order*, 8 FCC Rcd 5837 n.808 ("we do not think a cable operator can escape rate regulation simply by announcing that tiered services are available a la carte").

[29] *Second Reconsideration Order* ¶ 196.

[30] We are not precluding Paragon from treating this package as a cable programming service tier, priced pursuant to our rules, or from putting the channels back into an existing tier.

[31] *Going Forward Order* ¶ ¶ 16-37.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Century Cable TV LOI-93-49
Huntington, West Virginia

Letter of Inquiry

MEMORANDUM OPINION AND ORDER

Adopted: November 23, 1994; Released: November 25, 1994

By the Chief, Cable Services Bureau:

I. INTRODUCTION

1. The Commission received a Form 329 Complaint on November 15, 1993, concerning the reasonableness of the rates charged for cable programming services by Century Cable TV of Huntington, West Virginia ("Century"). In response to this complaint, the Commission issued Letter of Inquiry 93-49 ("LOI") to Century on December 13, 1993.[1] The LOI asked Century to provideinformation concerning its compliance with the Commission's rules governing evasion in the offering of packages which allegedly are not rate-regulated. Century responded to our LOI on January 12, 1994.

II. BACKGROUND

2. In the Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act"), Congress created a regulatory scheme giving the Commission and local franchising authorities jurisdiction over the cable programming and equipment rates of non-competitive cable systems. The 1992 Cable Act provides that the rates of cable systems not subject to effective competition may be regulated by local franchising authorities, in the case of basic service, and by the Commission, in the case of cable programming services.[2] A stated policy of the 1992 Cable Act is to ensure that "consumer interests are protected in the receipt of cable service."[3]

3. The 1992 Cable Act requires cable operators to offer subscribers a basic tier that must contain at least all qualified local broadcast signals and, unless otherwise specified by the local franchising authority, public, educational, and governmental channels.[4] The Commission was charged by the 1992 Cable Act with creating regulations that ensure that the rates for the basic service tier are reasonable.[5] The 1992 Cable Act directs that "[s]uch regulations shall be designed to achieve the goal of protecting subscribers of any cable system that is not subject to effective competition from rates for the basic service tier that exceed the rates that would be charged for the basic service tier if such cable system were subject to effective competition."[6] Under the 1992 Cable Act, operators may offer other channels in a cable programming service tier or tiers.[7] The 1992 Cable Act orders the Commission to create regulations for the cable programming service tiers that allow it to identify individual cases of unreasonable rates.[8] The 1992 Cable Act thus protects consumers' interests in continuing to receive the basic service tier and cable programming service tiers at reasonable rates.

4. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[9] The 1992 Cable Act's legislative history states that the Commission should scrutinize offerings of non-traditional stand-alone services to "prevent repricing, retiering, or other alterations of rate structures" that could have the effect of evading the purposes of rate regulation.[10] This provision in the 1992 Cable Act is intended to give the Commission the authority to address changes in the cable industry's business practices that would thwart the intent of rate regulation.[11]

5. In the *Rate Order* the Commission defined evasion as "any practice or action which avoids the rate regulation provisions of the Cable Act or Commission rules contrary to the intent of the Act or its underlying policies."[12] We must scrutinize a particular operator's marketing or pricing practices to determine whether those practices have the effect of avoiding the requirements of our rate regulations, contrary to the intent of the 1992 Cable Act and our rules.

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[1] Letter from Roy J. Stewart, Chief, Mass Media Bureau, FCC, to Century Cable TV of Huntington, West Virginia, LOI-93-49 (December 13, 1993). Copies of the Letter of Inquiry and Response are available to the public in the FCC's Cable Reference Center, 2033 M Street, N.W., Room 207, Washington, D.C. We also note that there is a pending rate complaint proceeding involving Century. Our decisions made herein will be made a part of that proceeding. Thus, for example, we will not order Century to make refunds to subscribers in regard to Century's purported "a la carte" restructuring. Obviously, however, we may order refunds if we find violations of other rules that should result in refunds.

[2] Communications Act of 1934 § 623 (a)(2), 47 U.S.C. § 543 (a)(2)(1992).

[3] Pub. L. No. 102-385 § 2 (b) (4) (1992); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. at 34 (1992).

[4] Communications Act of 1934 § 623 (b)(7)(A)(ii-iii), 47 U.S.C. § 543 (b)(7)(A)(ii-iii)(1992); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket 92-266, *Report and Order and Further Notice of Proposed Rulemaking*, 8 FCC Rcd 5631 ¶ 157-161 (1993) (*"Rate Order"*) (franchising authorities may require "operators to carry PEG channels on tiers other than basic).

[5] Communications Act of 1934 § 623 (b)(1), 47 U.S.C. § 543 (b)(1)(1992).

[6] *Id.*

[7] Communications Act of 1934 § 623(l)(2), 47 U.S.C. § 543(l)(2)(1992).

[8] Communications Act of 1934 § 623 (c)(1)(A), 47 U.S.C. § 543 (c)(1)(A)(1992). Identification of individual cases of unreasonable rates is achieved by a process in which the Commission assumes jurisdiction over systems where a complaint about a cable programming service tier rate is filed.

[9] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[10] H.R. Rep. No. 628, 102d Cong., 2d Sess. at 79 (1992).

[11] S. Rep. No. 92, 102d Cong., 2d Sess. at 77 (1992).

[12] *Rate Order* ¶ 451.

III. FACTS

6. Before September 1, 1993, Century's services included a 13 channel basic tier, called Basic Service, for $12.95 per month, a 13 channel cable programming service tier, called the Silver tier, for $7.00 per month, and an additional 7 channel cable programming service tier, called the Gold tier, for $2.00 per month. In order to receive the Gold tier, subscribers were required to purchase both the basic tier and the Silver tier.

7. The following chart summarizes Century's service tier offerings prior to September 1, 1993:

Offering	Channels	Price
1. Basic Service	13	$12.95
2. Silver tier	13	$7.00
3. Gold tier	7	$2.00
Total	33	$21.95

8. Beginning September 1, 1993, the date our rate regulations became effective, Century restructured its service offerings. Century's restructured service offerings included a 30 channel basic tier, called Basic Service, for $21.75 per month and three channels offered in an a la carte package, called Century Select. The three channels were Cable News Network (CNN), TBS, and Turner Network Television (TNT). TNT and CNN were originally in Century's Gold tier and TBS was originally in Century's basic tier.

9. CNN, TBS, and TNT could be purchased individually for $1.35 per month. All three channels could be purchased as a package for $3.00 per month.

10. The following chart summarizes Century's service tier options as of the date of its response to our LOI:[13]

Offering	Channels	Price
1. Basic Service	30	$21.75
2. Century Select	3	$3.00
Total	33	$24.75

11. Century states that there are no installation or other one-time charges necessary to receive the Century Select channels either individually or as a package. In addition, Century states that there are no downgrade or upgrade fees applied when subscribers switch from the package to individual channels or from individual channels to the package.

12. Century argues, *inter alia,* that it began offering its services individually and through the Century Select package in order to implement Congress' intent to maximize consumer choice. However, based on the record, very few consumers elected to exercise that choice. As of the date of its response, Century states that 323 subscriptions to individual channels were made, while 19,868 subscribers took the Century Select package.

IV. DISCUSSION

13. The 1992 Cable Act requires the Commission to adopt standards and guidelines to prevent evasions, "including evasions that result from retiering."[14] An evasion, as defined by the Commission, is an act or practice that "avoids the rate regulation provisions of the [Cable] Act or our rules contrary to the intent of the Act or its underlying policies."[15] In the *Rate Order,* we stated that "retiering otherwise permitted under our rules will not be deemed an evasion."[16] First, we examine whether Century's response to the LOI shows that its restructuring of its offerings had the effect of evading rate regulation for the channels that Congress intended to be rate-regulated.

14. Century's restructuring effective September 1, 1993, involved its movement of two channels (TNT and CNN) from its 7 channel Gold tier and one channel (TBS) from its 13 channel Basic Service to create the three-channel package that it alleges is not rate-regulated. Thus, Century removed channels from otherwise rate-regulated tiers to create a new package of channels. In so doing, Century avoided application of our rate regulations which generally required cable operators to reduce rates by about 10 percent. That is, if Century had not restructured on September 1, 1993, it would have been required to recalculate its rates in accordance with the *Rate Order* we released on May 3, 1993, which generally required cable operators to reduce their rates. Moreover, customers that were receiving the two Gold tier channels and the one Basic Service channel at issue continued to receive them after the restructuring, and there appears to be no sufficient justification for Century's restructuring other than to avoid rate regulation.

15. Other factors corroborate our view that Century's restructuring may have had the effect of avoiding rate regulation. First, it offered this package on the eve of regulation. Second, it automatically subscribed its customers to the offerings that previously had been part of its basic and cable programming service tiers. In light of these facts, it appears that Century's restructuring of its offerings may have evaded rate regulation. We will not find an actual evasion occurred, however, if Century's action complied with our a la carte policy that was in effect at the time of its restructuring. If the offering met our requirements for a permissible collective offering of a la carte channels, then Century would not have evaded our rate regulations because it would not be required to reduce its price for the collective a la carte package.[17]

16. In our *Rate Order,* the Commission recognized that "a la carte packages" appear to be "cable programming services," but said that "interpreting the statute in such a literal fashion could disadvantage consumers by denying them discounts on packages of per-channel or per-program services and by limiting subscriber access to a greater quantity of premium programming."[18] Thus, we envisioned that

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[13] This Order does not evaluate Century's rates for its Basic Service. These rates are subject to review by the local franchising authority in a separate proceeding.

[14] Communications Act of 1934 § 623(h), 47 U.S.C. § 543(h)(1992).

[15] *Rate Order* ¶ 451.

[16] *Id.* at ¶ 453.

[17] In our *Going Forward Order,* we have reconsidered our regulatory treatment of collective offerings of a la carte channels. *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking,* MM Docket Nos. 92-266 and 93-215, FCC 94-286 (adopted November 10, 1994) *("Going Forward Order").* Specifically, we have determined that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act and therefore will be subject to our general rate regulation rules. However, in order to determine whether Century evaded rate regulation when it restructured its offering, we must evaluate its a la carte package under the rules that were in effect when it restructured.

[18] *Rate Order* ¶ 329.

cable operators, for the most part, would offer channels that previously had been offered a la carte in discounted packages, and concluded that it would be better for consumers if we construed the 1992 Cable Act to permit such discounting.[19] This is not the type of offering that Century and others have provided their subscribers. Specifically, these operators did not offer a discounted package of channels that previously had been offered a la carte to subscribers, but instead removed channels from a tier that would be subject to our rate regulations.

17. Moreover, in the *Rate Order,* the Commission determined that such a la carte packages would be exempt from rate regulation, i.e., would be deemed not to fall within the definition of "cable programming service," if two conditions were met: (1) the price for the combined package must not exceed the sum of the individual charges for each component service; and (2) the cable operator must continue to provide the component parts of the package to subscribers separately in addition to the package. The Commission said that the second condition would be satisfied only when "the per channel offering provides consumers with a realistic service choice."[20]

18. Under the two-part test that we set forth in the *Rate Order,* it is clear, first, that the price for the combined package does not exceed the sum of the individual charges for the three services, because subscribers may purchase the three channels for $1.35 each or the three-channel package for $3.00. The second part of the test is whether the separate parts of the package constitute a "realistic service offering." The results of our review of Century's submission reveal that there were only 323 subscriptions to individual Century Select channels. Our test does not specify what number would indicate that an offering is "a realistic service offering." However, the fact that there were only 323 subscriptions to individual Century Select channels, together with the other factors present in this case,[21] tends to show, in this instance, that the per-channel offering does not constitute a realistic service offering.

19. Even if we were to apply the 15 interpretative guidelines set forth in our *Second Reconsideration Order,*[22] we still would not reach a clear answer to the question of what constitutes a realistic service offering. Although some factors support a finding that Century's offering was not a permissible a la carte package, other factors point the other way. In particular, although a "significant percentage" of the channels offered in the a la carte package (100 percent) was removed from regulated tiers, the absolute number (three) was small.[23] Moreover, our test does not explain how the factors are to be weighed against each other. In these circumstances, we cannot say that it was clear to Century that its restructuring was not a permissible a la carte package.

20. In our recently adopted *Going Forward Order,* we have reconsidered our rules relating to a la carte packages and concluded that such packages are cable programming service tiers within the meaning of Section 3(l)(2) of the 1992 Cable Act. For that reason, the package at issue is subject to rate regulation and cannot continue to be treated as an unregulated package of channels. In reaching this conclusion in the *Going Forward Order,* we acknowledged that, as applied to many fact patterns, we did not provide a clear test in the *Rate Order* and the *Second Reconsideration Order* for determining whether an a la carte package was permissible. In adopting the 15 interpretive guidelines in the *Second Reconsideration Order* to supplement the *Rate Order's* two-prong test, we hoped to enable operators to better determine what collective offerings of a la carte channels would be considered a realistic service offering, and, hence, not an evasion of rate regulation.[24] Our experience to date, however, indicates that our efforts did not produce the intended result and that, instead, there has been confusion as to whether collective offerings of a la carte channels constituted an evasion of rate regulation. Indeed, we cannot say that it is clear that Century's restructuring was not a permissible a la carte package.

21. For that reason, we do not think that it would be equitable to subject Century to refund liability. This result is distinguishable from the result we reached in *Adelphia Cable Partners, L.P.,*[25] in which we determined that we will require refunds if Adelphia's rate justification proceedings show that subscribers' rates were higher than our rules permitted. In that case, the cable operator announced that it would offer all the channels previously offered on a cable programming service tier on an individual basis or as a collective offering of a la carte channels. In so doing, Adelphia removed an entire service tier from rate regulation, while here, Century eliminated two cable programming service tiers but moved most of the channels from those tiers into the rate regulated basic tier. Century attempted to treat only three channels as an unregulated collective offering of a la carte channels. Moreover, while we have indicated above that our rules for determining whether collective offerings of a la carte channels constitute an evasion were in many instances difficult to apply, we do not believe that our a la carte rules are unclear as applied to the fact pattern in the *Adelphia* case. In the *Rate Order,* we stated that a cable operator could not escape rate regulation simply by calling what otherwise would be a

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[19] *See, e.g., Rate Order* ¶ 453 n.1161 ("There is no evidence that operators would or, as a business matter, could shift programming previously offered as part of a tier to 'a la carte' status, *i.e.,* a per-channel or per-program offering, to avoid the rate regulation applicable to tiers").

[20] *Id.* at ¶ ¶ 327-28 & n.808. In the *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-266, *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking,* 9 FCC Rcd 4119 (1994) (*"Second Reconsideration Order"),* the Commission affirmed its prior view. It said that "we continue to believe that the public interest will be served by generally permitting non-regulated treatment of collective offerings of 'a la carte' channels if the offering enhances consumer choice and does not constitute an evasion of rate regulation." *Id.* at ¶ 194. In this regard, we retained the two-part test contained in the *Rate Order* for determining when we would refrain from regulating "a la carte packages." In addition, the Commission set out 15 guidelines to enable operators to better determine what collective offerings of "a la carte" channels will be considered "realistic service offerings." *Id.* at ¶ 195.

[21] *See, e.g.,* ¶ ¶ 14-15, *supra.*

[22] *Second Reconsideration Order* at ¶ 196.

[23] *Id.*

[24] *See Going Forward Order* ¶ 40.

[25] *Adelphia Cable Partners, L.P.,* South Dade County, Florida, LOI-93-42, FCC 94-1277 (released November 18, 1994).

rate regulated tier an a la carte package.[26] We reiterated this admonition in the *Second Reconsideration Order* when we warned against eliminating "an entire regulated tier" and "turning it into an a la carte package."[27]

22. We will not require Century to restructure its tiers so as to return the channels offered in the a la carte package to the basic or cable programming service tiers,[28] instead, on a prospective basis, therefore, we will consider Century's collective offering of a la carte channels a new product tier[29] even though it would not qualify as a new product tier under our recently announced *Going Forward Order* because one of the conditions for a new product tier is that channels may not be removed from a basic service tier or a cable programming service tier. In light of the prior confusion over what constituted a permissible a la carte offering, and because Century's three-channel tier, unlike Adelphia's offering, did not constitute a clear evasion of our rate rules, we see no good reason to subject Century or its Huntington customers to the confusion and transaction costs that would result if we required Century to retier.

V. ORDERING CLAUSES

23. Accordingly, IT IS ORDERED that Century's package as it existed on January 14, 1994, may be treated as a new product tier under our *Going Forward Order*.

24. IT IS FURTHER ORDERED that this Order is EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

[26] *Rate Order*, 8 FCC Rcd 5837, n.808 ("we do not think a cable operator can escape rate regulation simply by announcing that tiered services are available a la carte").
[27] *Second Reconsideration Order* ¶ 196.
[28] We are not precluding Century from treating this package as a cable programming service tier, priced pursuant to our rules, or from putting the channels back into an existing tier.
[29] *Going Forward Order* ¶ ¶ 16-37.

Before the
Federal Communications Commission
Washington, D.C. 20554

Gen. Docket No. 88-476

In the Matter of

New York Metropolitan Area
Public Safety Plan

ORDER

Adopted: November 28, 1994; Released: December 9, 1994

By the Acting Chief, Land Mobile and Microwave Division and the Acting Chief, Spectrum Engineering Division:

1. The Private Radio Bureau and the Office of Engineering and Technology, acting under delegated authority, accepted the New York Metropolitan Area (Region 8) Public Safety Plan (Plan) on May 12, 1989, 4 FCC Rcd 4457 (1989).

2. By letter dated July 11, 1994, the Region proposed to amend its Plan. The proposed amendment would revise the current channel allotments. The Commission placed the letter on Public Notice for comments due on November 4, 1994, 59 FR 50761 (October 5, 1994), and received no comments.

3. We have reviewed the proposed amendment to the Region 8 Plan and, having received no comments to the contrary, conclude it furthers the interests of the eligible entities within the Region.

4. Accordingly, IT IS ORDERED, That the Public Safety Radio Plan for the New York Metropolitan Area (Region 8) IS AMENDED, as set forth in the Region's letter of July 11, 1994. This Amendment is effective immediately.

FEDERAL COMMUNICATIONS COMMISSION

Rosalind K. Allen
Acting Chief, Land Mobile
and Microwave Division

Lawrence P. Petak
Acting Chief, Spectrum Engineering
Division

Before the
Federal Communications Commission
Washington, D.C. 20554

In re Applications of

ROCK PORT R-II SCHOOLS
Peru, Nebraska — File No. BPLIF-920501DK

BEATRICE CITY SCHOOL DISTRICT 15
Tecumseh, Nebraska — File No. BPLIF-930416DU

For Construction Permit and License
in the Instructional Television
Fixed Service on Channels G1, G2,
G3, and G4.

MEMORANDUM OPINION AND ORDER

Adopted: November 28, 1994; Released: December 9, 1994

By the Commission:

1. The Commission has before it for consideration the above-captioned mutually exclusive applications of Rock Port R-II Schools (Rock Port) and Beatrice City School District 15 (Beatrice), each seeking a construction permit and license in the Instructional Television Fixed Service (ITFS) on Channels G1-G4 in the areas of Peru and Tecumseh, Nebraska, respectively.

BASIC ELIGIBILITY

2. Before applying the mutually exclusive selection procedure to determine the number of merit points to be awarded to each applicant, we must first ascertain the basic eligibility of the applicants. Educational institutions and governmental organizations that propose to serve either their own enrolled students or students at accredited schools within their respective jurisdictions establish their eligibility by accreditation from the appropriate state department of education or a recognized regional or national accrediting organization. Other ITFS applicants that propose to serve students at accredited schools outside of their respective jurisdictions must, to be eligible, submit letters of intended use from those schools and establish local program committees in those communities. See 47 C.F.R. Section 74.932(a)(1)-(5). Each applicant is qualified to be an ITFS licensee. Both applicants are school systems that propose to provide formal educational programming to schools within and outside of their respective jurisdictions. Rock Port is accredited by the Missouri Department of Elementary and Secondary Education, whereas Beatrice is accredited by the Nebraska Department of Education.

MUTUALLY EXCLUSIVE SELECTION PROCEDURE

3. In cases of mutually exclusive ITFS applications, where applicants are competing for the same or adjacent channels in the same geographic area, each application is reviewed pursuant to our comparative process. This procedure awards a maximum of twelve merit points based on five criteria deemed to be most relevant to predicting the applicant best qualified to provide the service for which the ITFS spectrum has been allocated. *Instructional Television Fixed Service - Second Report and Order in MM Docket No. 83-523, (Second Report and Order)*, 101 FCC 2d 49, 65-72 (1985); 47 C.F.R. Section 74.913. First, four points are awarded to local applicants.[1] Second, three points are awarded to applicants which are accredited schools, educational institutions, or school boards and school districts applying within their jurisdictions. Third, two points are awarded to applicants whose requests would result in the acquisition by these applicants of four or fewer ITFS channels within the particular area. Fourth, either one or two points may be awarded to applicants for specified levels of proposed ITFS programming.[2] Fifth, one point is awarded to applicants which are existing E or F channel licensees seeking to relocate on another ITFS channel group, where such applicants show an established need for an expanded service that cannot be accommodated on their grandfathered E or F facilities. The tentative selectee is the applicant with the highest score.

4. Under this comparative selection process, the applicants are awarded points based on the following criteria:

Localism. Each applicant is entitled to four points for being local. Rock Port and Beatrice are school systems serving the formal educational needs of schools within their own jurisdictions.

Accreditation. Each applicant is entitled to three points for being accredited. Rock Port is accredited by the Missouri Department of Elementary and Secondary Education. Beatrice is accredited by the Nebraska Department of Education.

Four-Channel Limitation. Neither applicant is the licensee of, or has filed applications for, additional ITFS channels in its proposed service area. Therefore, each applicant is entitled to two points for remaining within the four-channel limitation.

Instructional Programming. ITFS applicants detail their formal educational and other ITFS programming proposals in both a program schedule and a program "grid." Rock Port's illustrative schedule and programming grid propose an average of 24.375 hours of formal educational programming per channel per week. Therefore, Rock Port is en-

[1] A "local" applicant is an institution or organization that is physically located in the community or metropolitan area where service is proposed. *Second Report and Order*, 101 FCC 2d at 59; 47 C.F.R. Section 74.932, Note 1.

[2] One point is awarded for a proposed weekly schedule of at least 21 average hours per channel of formal educational programming or of at least 41 average hours per channel of other ITFS programming. Two points are awarded for a proposed weekly schedule of at least 41 average hours per channel of formal educational programming or at least 61 hours per channel of ITFS programming where at least 21 of those hours are formal educational programming. 47 C.F.R. Section 74.913(b)(4).

titled to one programming merit point. In constrast, Beatrice's illustrative schedule and grid propose an average of 42 hours of formal educational programming per channel per week. Therefore, Beatrice is entitled to two programming merit points.

E- and F- Channel Group Relocation. Neither applicant is the current licensee of an E or F channel seeking to relocate to other channels. Consequently, neither is entitled to the one point for such applicants.

Total. Rock Port is entitled to four points for being local, three points for being accredited, two points for observing the four-channel limitation, and one point for proposing at least 21 hours of formal educational ITFS programming per channel per week, for a total of ten points. Beatrice is entitled to four points for being local, three points for being accredited, two points for observing the four-channel limitation, and two points for proposing at least 41 hours of formal educational ITFS programming per channel per week, for a total of eleven points. Thus, the tentative selectee is Beatrice.

OTHER MATTERS

5. No determination has been made that the tower heights of four of the receive sites proposed by Beatrice would not constitute a hazard to air navigation. Accordingly, any grant of a construction permit/license to Beatrice will be appropriately conditioned. See *Bells Independent School District*, 9 FCC Rcd 1551, 1552 (1994).

6. Beatrice proposes to lease excess capacity for non-ITFS use as permitted by Section 74.931, and has submitted a copy of the lease agreement it executed with U.S.A. Wireless, Inc. (USA). The lease agreement does not, however, conform entirely to the Commission's requirements for such agreements. Specifically, in the event that Beatrice and USA are unable to reach agreement on additional renewal terms, the lease provides for the continued operation by USA on the licensed channels for a six-month period beyond Beatrice's license term. This provision is inconsistent with the Commission's maximum term for excess capacity leases. See *Instructional Television Fixed Service - Report and Order in Gen. Dockets Nos. 90-54 and 80-113*, 5 FCC Rcd 6410, 6416 (1990); and *Mooreland Public Schools*, 9 FCC Rcd 527, 528 (1994). Although this provision is inconsistent with our requirements for excess capacity leases, it neither reflects on the applicant's basic or comparative qualifications nor precludes grant of an authorization. See *Van Vleck Independent School District*, 7 FCC Rcd 7231, 7233 (1992). Accordingly, Beatrice's authorization will be conditioned upon conformity of the lease to Commission requirements.

7. No petitions to deny or informal objections have been filed against Beatrice's application, and we find Beatrice fully qualified to be an ITFS licensee. We also conclude that grant of its application would serve the public interest, convenience and necessity.

8. Accordingly, IT IS ORDERED, That the application of Rock Port R-II Schools (BPLIF-920501DK), IS DENIED, and the application of Beatrice City School District 15 (BPLIF-930416DU) IS GRANTED, subject to the condition that within 30 days from the release date of this Order, Beatrice City School District 15 submits to the Chief, Distribution Services Branch, for approval information demonstrating compliance with Commission requirements, including, if appropriate, an amended excess capacity lease conforming in the manner discussed herein.

9. IT IS FURTHER ORDERED, That the authorization issued to Beatrice Independent School District 15 shall be conditioned as follows: This authorization is subject to the condition that construction of the receive towers at receive site locations R-1, R-2, R-5, and R-7 is prohibited until clearance is received from the Federal Aviation Administration, the Commission is so notified, and the appropriate painting and lighting specifications are determined.

10. IT IS FURTHER ORDERED, That the staff of the Mass Media Bureau shall send copies of this decision to the applicants by certified mail, return receipt requested.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

DA 94-120

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C 20554

In the Matter of	)	
	)	
Implementation of Section 17	)	
of the Cable Television	)	ET Docket No. 93-7
Consumer Protection and	)	
Competition Act of 1992	)	
	)	
Compatibility Between	)	
Cable Systems and Consumer	)	
Electronics Equipment	)	

ORDER EXTENDING TIME FOR REPLY COMMENTS

Adopted: February 3, 1994 ; Released: February 4, 1994

Reply Comment Date: February 16, 1994

By the Chief Engineer:

1. On February 2, 1994, the Consumer Electronics Group of the Electronics Industries Association (EIA/CEG) requested that the Commission extend the time for filing reply comments in response to the Notice of Proposed Rule Making in the above captioned proceeding, FCC 93-495, released December 1, 1993, by one week, to February 16, 1994.

2. In its request, the EIA/CEG states that a one week extension of the period for filing reply comments is needed because the current 15-day filing period does not allow enough time to prepare adequate responses to the first round comments. The EIA/CEG indicates that the task of preparing responses in this short period is complicated by the number, length and diversity of the comments and the time needed to obtain and distribute copies of comments to its member companies.

3. The Commission does not routinely grant extensions of time.[1] Moreover, in this instance time is especially important, as the Commission has a statutory deadline to adopt rules for assuring compatibility by April 3, 1994. Nonetheless, we agree with the EIA/CEG that the volume and diversity of the comments warrants additional time for preparing replies. We believe the relatively brief 7-day extension that the EIA/CEG requests is consistent with both the task of preparing comments and our need

[1] See 47 C.F.R. §1.45 (1991).

to complete this matter expeditiously. Accordingly, IT IS ORDERED THAT the time for filing reply comments IS EXTENDED to February 16, 1994.

3. This action is taken pursuant to authority found in Sections 4(i) and 303 of the Communications Act of 1934, as amended, 47 U.S.C. Sections 154(i) and 303, and pursuant to 47 CFR Sections 0.31, 0.241, and 1.46. For further information, contact Alan Stillwell, Office of Engineering and Technology, (202) 632-7060.

Federal Communications Commission

Thomas P. Stanley
Chief Engineer

PUBLIC NOTICE

FEDERAL COMMUNICATIONS COMMISSION
1919 M STREET N.W.
WASHINGTON, D.C. 20554

DA 94-206

News media information 202/632-5050. Recorded listing of releases and texts 202/632-0002.

March 7, 1994

APPLICATION OF EX PARTE RULES TO PROCEEDINGS INVOLVING ROGERS COMMUNICATIONS INC. AND MCLEAN HUNTER LIMITED

Pending before the Commission are the applications listed below for consent to the transfer of control of the identified CARS licenses.

Applications for consent to transfer control and for special temporary authority to transfer control from the shareholders of Mclean Hunter Limited to Pierre Juneau, P.C., O.C., Trustee, filed on a supplemented FCC Form 327:

CAR-44473-09 WGV-931 Selkirk Communications, Inc.
Hallandale, Florida

CAR-44474-09 WGV-930 Selkirk Communications, Inc.
Fort Lauderdale, Florida

CAR-44475-09 KA-80605 Selkirk Communications, Inc.
Hallandale, Florida

CAR-44476-09 WHZ-792 Mclean Hunter Cable TV, Inc.
Taylor, Michigan

CAR-44477-09 WHZ-300 Cablevision of New Jersey, Inc.
Elizabeth, New Jersey

CAR-44478-09 WHZ-473 Barden Cablevision
Detroit, Michigan

CAR-44479-09 KC-7712 Suburban Cablevision
Verona, New Jersey

CAR-44480-09 KA-2103 Suburban Cablevision
Near West Orange, New Jersey

Applications for consent to the transfer of control from the shareholders of Mclean Hunter Limited to Rogers Communications, Inc., FCC Form 327, filed by Diane S. Killory, Esq., and Warren Lavey, Esq.:

CAR-44481-09 WGV-931 Selkirk Communications, Inc.
Hallandale, Florida

CAR-44482-09 WGV-930 Selkirk Communications, Inc.
Fort Lauderdale, Florida

CAR-44483-09 KA-80605 Selkirk Communications, Inc.
Hallandale, Florida

CAR-44484-09 WHZ-792 Mclean Hunter Cable TV, Inc.
Taylor, Michigan

CAR-44485-09 WHZ-300 Cablevision of New Jersey, Inc.
Elizabeth, New Jersey

CAR-44486-09 WHZ-473 Barden Cablevision
Detroit, Michigan

CAR-44487-09 KC-7712 Suburban Cablevision
Verona, New Jersey

CAR-44488-09 KA-2103 Suburban Cablevision
Near West Orange, New Jersey

Each of the listed licensees is a subsidiary or joint venture of Mclean Hunter Limited ("Mclean Hunter"), which is the subject of a hostile tender offer. Rogers Communications Inc. ("Rogers"), seeks to acquire two-thirds of the stock of Mclean Hunter. In accord with the Commission's two-step approval process for tender offers, Rogers has filed supplemented "short-form" applications, FCC Form 327, and requests for special temporary authority (STA) seeking Commission consent to the transfer of the CARS licenses to a Trustee who would acquire and vote, subject to certain restrictions, the stock obtained via the tender offer. The Trustee would exercise control of the licensed facilities pending Commission review of the second step in the two-step tender offer process, the "long-form" applications for consent to the transfer of the CARS licenses to Rogers.

None of the listed applications has yet been formally opposed, rendering them exempt at this point from ex parte limitations under Section 1.1204(a) of the Commission's Rules. However, in view of the expectation that these applications will be formally opposed because of the status of the proposed acquisition as a hostile tender offer, we have determined that all proceedings connected with the above-referenced applications should be restricted within the meaning of our ex parte rules. See 47 C.F.R. §§ 1.1200(a) and 1.1208. Accordingly, ex parte presentations made to or from decision-making personnel in any of the proceedings listed above are prohibited until the Commission's final dispositions of all the proceedings are no longer subject to reconsideration or judicial review. Parties to any one of the proceedings shall, for purposes of the ex parte rules, be deemed to be parties to all of the proceedings.

This action is taken by the Acting Chief, Cable Services Bureau. For further information, contact Rebecca L. Dorch (202)416-1169.

PUBLIC NOTICE

FEDERAL COMMUNICATIONS COMMISSION
1919 M STREET N.W.
WASHINGTON, D.C. 20554

News media information 202/632-5050. Recorded listing of releases and texts 202/632-0002.

DA 94-240

March 16, 1994

APPLICATION OF EX PARTE RULES TO INTERNET E-MAIL

The Commission's new computer system now affords members of the public access to decision-making personnel through delivery of Internet E-Mail. The purpose of this public notice is to remind the public that the ex parte rules (47 C.F.R. §1.1200 et seq.) that apply to written presentations to any Commission decision-making personnel also apply to Internet E-Mail presentations.

In restricted proceedings (e.g., proceedings involving mutually exclusive applications, a formal complaint, or a formally opposed application), oral and written ex parte presentations are generally prohibited. See 47 C.F.R. §1.1208. Therefore, as with other written presentations, Internet E-Mail presentations to Commission decision-makers in restricted proceedings are prohibited unless they are served on all parties to the proceeding.

In non-restricted proceedings (e.g., most informal rulemakings after issuance of a notice of proposed rulemaking), ex parte presentations are permissible (except during the Sunshine Period) but must be disclosed. See 47 C.F.R. §1.1206. Therefore, as with other written presentations, if an Internet E-Mail ex parte presentation in a non-restricted proceeding is transmitted to any decision-making personnel, two hard copies of that presentation should be provided to the Secretary. The presentation (as well as any transmittal letter) should indicate clearly on its face the docket number of the particular proceeding(s) to which it relates and the fact that two copies of it have been submitted to the Secretary. The presentation should be labeled or captioned as an ex parte presentation. See 47 C.F.R. §1.1206(a)(1).

During the Sunshine Period (the period which commences when an item is placed on the Sunshine Agenda and ends when the item is released), unless specifically exempted, all presentations concerning an item on the Sunshine Agenda, ex parte or not, are prohibited. See 47 C.F.R. §1.1203. This prohibition applies whether the proceeding is restricted, non-restricted, or is exempt under the ex parte rules. Therefore, unless an exemption specifically applies (e.g., a presentation specifically requested by the Commission or staff or a presentation from Congress or another Federal Government agency, see 47 C.F.R. §1.1203(b)&(c)),

no Internet E-Mail presentations should be transmitted during the Sunshine Period to decision-making personnel. See 47 C.F.R. §1.1203.

Action by the General Counsel.

For further information, contact Steve Bailey (202) 254-6530.

FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

DA 94-287

In re Applications of	)	
	)	
ROGERS COMMUNICATIONS INC.	)	File Nos. CAR-44475-09, CAR-44476-09,
	)	CAR-44478-09 to CAR-44480-09,
	)	CAR-44506-09 to 44511-09
For Consent to Interim	)	
Transfer of Control of	)	
Maclean Hunter Limited	)	
	)	

MEMORANDUM OPINION AND ORDER

Adopted: March 30, 1994 **Released: March 30, 1994**

By the Acting Chief, Cable Services Bureau:

1. Rogers Communications Inc. ("Rogers"), seeks to acquire control by tender offer of Maclean Hunter Limited ("Maclean"), which, through various subsidiaries, holds Commission licenses for cable television relay service stations.[1] Rogers filed applications on March 1, 2, 14, 16 and 25, 1994,[2] seeking to utilize the two-step procedure for FCC approval of the transfer of control of a company subject to a tender offer, as authorized in the Commission's 1986 Policy Statement in Tender Offers and Proxy Contests, 59 RR

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[1] Rogers Communications Inc., and its various affiliates, subsidiaries and interests are referred to hereinafter collectively as Rogers. Maclean Hunter Limited and its various affiliates, subsidiaries and interests involved in the tender offer are referred to hereinafter collectively as Maclean.

[2] On March 1 and 2, 1994, Rogers filed "short-form" FCC Form 327 applications with respect to eight CARS licenses, with requests that the Commission grant special temporary authorization to Rogers' trustee to acquire and vote the shares of Maclean acquired through the tender offer. On March 1, 1994, Rogers filed "long-form" FCC Form 327 applications seeking Commission consent to transfer of control of these same eight CARS licenses to Rogers. On March 17, 1994, the "short form" applications and STA requests for three of these CARS licenses were withdrawn because Maclean either was not the licensee or the licenses had been cancelled. On March 22, 1994, the "long-form" applications pertaining to these same three CARS licenses were withdrawn. On March 14, 1994, Rogers filed "long-form" FCC Form 327 applications seeking Commission consent to the transfer of control of six additional CARS licenses to Rogers. On March 16, 1994, Rogers filed "short-form" FCC Form 327 applications and STA requests with respect to the additional six CARS licenses and on March 25, 1994, refiled the STA requests (which had been returned) for the six additional CARS licenses.

2d 1536 (1986), appeal dismissed sub nom. Office of Communication of the United Church of Christ v. FCC, 826 F. 2d 101 (DC Cir. 1987). In accordance therewith, Rogers filed FCC Form 327 applications, with requests that the Commission grant special temporary authorization (STA) to a trustee to enable the trustee to acquire and vote, subject to certain restrictions, the Maclean shares obtained via the tender offer and to exercise control of Maclean should Rogers' tender offer prevail, during the interim period when Rogers' qualifications are under consideration.[3]

BACKGROUND

2. Rogers is a Canadian communications company engaged, through various subsidiaries, in cellular and other wireless communications, cable television, and radio and television broadcasting in Canada. Through an affiliate, Rogers Cablesystems of Alaska, Rogers indirectly owns a cable television system near Anchorage, Alaska which serves the Anchorage suburbs of Palmer, Wassilla and portions of Matanuska-Susitna Burrough.

3. Maclean is a publicly and widely traded diversified communications company with interests throughout North America and in Europe. Maclean is engaged in periodical publishing, cable television, radio and television broadcasting, commercial printing, radio paging, media monitoring, and trade and consumer shows. Maclean also has a controlling interest in several newspapers in Canada and the United States. Through subsidiaries, Maclean holds Commission licenses for cable television relay service ("CARS") stations for use in connection with its cable businesses in Florida, Michigan and New Jersey.[4] Maclean is incorporated under the laws of the Province of Ontario.

4. Maclean is subject to information and reporting requirements of the Ontario Business Corporations Act, as amended, the securities laws of certain provinces of Canada, and the rules of the Toronto Stock Exchange and the Montreal Exchange. Maclean must comply with certain regulatory requirements of the Canada Broadcasting Act, the Competition Act, and the Canadian Radio-television and Telecommunications Commission ("CRTC"). Maclean

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[3] For the step one applications, i.e., the "short-form" applications and STA requests, see FCC File Nos. CAR-44475-09, CAR-44476-09, CAR-44478-09 to CAR-44480-09, CAR-44506-09 to 44511-09. For the step two applications, i.e., the "long-form" applications, see File Nos. CAR-44483-09, CAR-44484-09, CAR-44486-09 to CAR-44488-09, CAR-44512-09 to 44517-09.

[4] These CARS station licenses involved in this transaction are: KA-80605, Hallandale, FL; WHZ-792, Taylor, MI; WHZ-473, Detroit, MI; KC-7712, Verona, NJ; KA-2103, Near West Orange, NJ; KB-60216, Near Woodbridge, NJ; WBM-749, New York, NY; WGV-838, East Brunswick, NJ; WHZ-461, East Brunswick, NJ; WHZ-462, Woodbridge, NJ; and WLY-202, Jersey City, NJ.

Maclean also holds Commission business radio and operational fixed service station licenses and has requested similar treatment of those applications. It is noted that the Private Radio Bureau is today granting the STA requests pertaining to OFS Call Signs WNEZ859, WNEZ858, WNEU606, WNEU605, WNEU603 and WNEU604 at Detroit, MI; and Business Radio Station Call Signs WSG388 at Taylor, MI, WNQT900 at East Detroit, MI, WNIC391 at Detroit, MI, KQ4869, KA62612, WNRR898 at Fort Lauderdale, MI, KWZ466 and KNBT323 at Union, MI.

is also obligated to comply with certain regulatory, information and reporting requirements of the United States Securities and Exchange Commission, as provided in the Multijurisdictional Disclosure System, the United States Federal Trade Commission and the United States Department of Justice through the Hart-Scott-Rodino Antitrust Improvements Act of 1976,[5] and the Federal Communications Commission and various U.S. state and local municipalities through the United States Communications Act of 1934, as amended.[6]

5. Pursuant to regulations made under the Canadian Broadcasting Act, a change in the effective control of licensed broadcasting undertakings, or the acquisition of 30% or more of the voting shares of the undertaking or of a person which has effective control of the undertaking, requires the prior approval of the CRTC. See Roger's Form F-8, Circular at 24. Because Maclean is licensed by the CRTC to operate cable systems and television and radio stations in Canada, prior approval of the CRTC must be obtained before Rogers can effectuate its tender offer. Id. As discussed more fully below, pursuant to the U.S. Communications Act of 1934, as amended, and the Commission's Rules, because Maclean holds CARS licenses utilized in the operation of its U.S. cable businesses, prior approval of the FCC must also be obtained before Rogers can effectuate its tender offer. In order to allow the shares deposited under the tender offer to be taken up pending receipt of the requisite approvals of the CRTC and the FCC, and all requisite approvals of U.S. state and municipal authorities to the transfer of the cable franchises, Rogers proposes to place the shares taken up and paid for under the tender offer into a trust to be controlled by Pierre Juneau, P.C., O.C. On March 17, 1994, the CRTC approved the appointment of Juneau as trustee of the shares of Maclean.[7]

6. According to the Form F-8 filed with the U.S. Securities and Exchange Commission and Canadian securities materials filed with the Commission by Rogers, principals of Rogers and Maclean began to explore the concept of a strategic merger in the form of a tender offer in January of 1994, at the behest of Rogers. Rogers had at that time acquired approximately 8.3% of Maclean's publicly held shares through open market transactions. Maclean had previously announced an intention to review options with respect to its U.S. cable businesses, including a possible sale of such systems. In early February, 1994, Rogers requested that Maclean not take any action with respect to its U.S. or Canadian cable businesses.

7. Notwithstanding initial efforts to pursue a consensual business combination, the parties were unable to agree upon terms and Rogers sought an

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[5] The requisite waiting period under regulations implementing the Hart-Scott-Rodino Antitrust Improvements Act has expired. Relevant portions of Rogers' Premerger Notification, as filed with the U.S. Department of Justice and the Federal Trade Commission on February 17, 1994, were submitted to the Commission on March 11, 1994.

[6] This list of Canadian and American statutes and regulations to which Maclean is subject is not intended to be exhaustive.

[7] A copy of the CRTC's approval was submitted to the Commission on March 18, 1994.

injunction from the Ontario Stock Exchange prohibiting Maclean from selling a significant block of stock to a third party. Rogers announced the principal terms of the tender offer on February 11, 1994, and on February 14, 1994, formally issued a tender offer to purchase all of the shares of Maclean at $17.00 cash and one Participating Right per common share.[8] The tender offer is valued at approximately $3 billion. Rogers' tender offer is contingent upon at least two-thirds of Maclean's outstanding shares being deposited. Pursuant to Canadian securities regulations, shareholders are permitted to withdraw tendered shares if such shares are not taken up and paid for by the offeror within 45 days of the initial tender offer.[9]

8. On February 15, 1994, the Board of Directors of Maclean announced that it had determined that the Rogers bid was unacceptable. The parties were unable to negotiate a mutually agreeable confidentiality agreement and on February 22, 1994, Rogers commenced a court action in Canada seeking an order granting it access to confidential information relating to Maclean. On February 23, 1994, Maclean issued a Directors' Circular formally recommending that Maclean shareholders not tender their shares. Maclean further announced that it was continuing to consider all strategic alternatives, including seeking a higher bid for all of the shares, the formation of strategic alliances and a recapitalization proposal.

9. Rogers' tender offer initially was set to expire on March 15, 1994. On March 8, 1994, Rogers and Maclean executed a letter agreement pursuant to which, among other matters, Rogers agreed to increase its bid price to $17.50 per share, without Participating Rights; Maclean agreed to recommend acceptance of the amended bid to its shareholders but reserved the right to change its recommendation; and the parties agreed to extend the bid by fifteen days and expressly recognized that time was of the essence. On March 11, 1994, Rogers issued an amended tender offer in accord with the March 8, 1994 letter agreement. Among other terms, the amended tender offer expires on March 31, 1994, limits the conditions under which the amended offer can be extended, further limits any such extension to a date no later than April 30, 1994, and permits Maclean's Board to consider, in accordance with its fiduciary obligations, unsolicited offers or proposals received from another party which provide a financially superior transaction. Also in accord with the March 8, 1994, letter agreement, Maclean issued a revised Directors' Circular on March 17, 1994, recommending acceptance of Rogers' amended tender

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[8] All dollar amounts referred to herein are to Canadian currency. The Participating Rights provision envisioned an entitlement to a *pro rata* share of the net proceeds from the sale of Maclean's U.S. cable businesses in excess of Cdn. $1.5 billion (the estimated value of the U.S. cable systems according to Rogers as of the date of the initial offer).

[9] See Canadian Securities Act, R.S.O. 1990, c. S.5, as amended by S.O. 1992, c.18, s.56, §§ 95(4) and 98. In contrast, in the U.S., pursuant to the Williams Act and SEC regulations, shareholders who have tendered shares in response to a tender offer are permitted to withdraw their tendered shares at any time after 60 days from the commencement of the tender offer. 15 U.S.C. §78n(d)(5) (1982); 17 CFR §240.14d-6(e)(v)(1985). See also Tender Offers and Proxy Contests, supra, 59 RR 2d at 1555. Cf. 17 CFR § 240.14d-7(a)(tendered shares may be withdrawn during the period the tender offer remains open).

offer.[10]

TRANSFERS OF CONTROL AND THE COMMISSION'S TENDER OFFER POLICY

10. Under Section 310 of the Communications Act of 1934, as amended, prior Commission consent to the transfer of control of a station license required under the Communications Act must be obtained. See 47 U.S.C. § 310(d). The Commission is empowered, however, under Section 309(f) of the Communications Act to grant special temporary authorizations if it finds that there are "extraordinary circumstances requiring temporary operations in the public interest and that delay in the institution of such temporary operations would seriously prejudice the public interest." 47 U.S.C. § 309(f). The Commission has found on several occasions in the past ten years that tender offer situations warrant utilization of special temporary authorizations. See, e.g., QVC Network, Inc., 8 FCC Rcd 8485 (1993); Macfadden Acquisition Corp. (Macfadden II), 60 RR 2d 872 (1986,. In L.P. Media, Inc., 102 FCC 2d 1276, 1285 (1985), the Commission found that "it is the circumstances presented by the tender offer itself that are 'extraordinary,' because of the need for expedition to permit shareholders to consider the tender offer." The Commission codified its position in its Policy Statement in Tender Offers and Proxy Contests, supra, 59 RR 2d at 1570-71, further finding that:

> [The criteria of Section 309(f)] are met in the exceptional situation in which a tender offer is used as a means to obtain control of a communications corporation. . . . The existence of . . disparate and potentially conflicting regulatory schemes presents an extraordinary circumstance which warrants the use of special procedures. Without the use of an expedited procedure which provides temporary authorization to the trustee, our regulatory processes would effectively result in precluding the use of tender offers as a means by which to obtain control over communications companies. This, in turn, would deprive shareholders of these companies of the ability to consider tender offers.

Tender Offers and Proxy Contests, supra, 59 RR 2d at 1570.[11]

11. One of the primary factors prompting the FCC's decision to adopt

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[10] Maclean's March 17, 1994, Notice of Change to Directors' Circular was submitted to the Commission on March 24, 1994.

[11] Prior to the issuance of the Policy Statement, the Commission granted STAs pursuant to the authority contained in Section 309(f) of the Communications Act in the context of hostile tender offers in L.P. Media, Inc., supra, 102 FCC 2d 1276 and One Two Corp., 58 RR 2d 924 (1985). See also Telesis Corporation, 68 FCC 2d 696 (1978)(STA granted to transfer control of fund holding controlling interest in a Commission licensee of CARS licenses to a new fiduciary following allegations and governmental investigations of alleged mismanagement). Cf. Westinghouse Broadcasting Company, Inc., 84 FCC 2d 938 (1981) (Group W permitted to acquire, and hold in a trust, less than a controlling interest in the stock of Teleprompter Corporation pending Commission action on transfer of control applications in connection with the friendly merger).

the Policy Statement was the need to resolve conflicts between federal laws and policies, in particular to resolve tensions between the Communications Act and the provisions of the Williams Act and the Securities and Exchange Act governing tender offers and shareholders' rights, and to accommodate the sometimes competing concerns of those Acts and the Hart-Scott-Rodino Act, the Sherman Act, and federal bankruptcy laws. Tender Offers and Proxy Contests, supra, 59 RR 2d at 1539-40. While the Commission has a duty to implement the Communications Act, it must do so in a manner as consistent as possible with other federal policies. See, e.g., Storer Communications, Inc. v FCC, 763 F.2d 436, 443 (DC Cir. 1985). The Policy Statement, and the procedures adopted therein, are "intended to provide a framework for the regulatory treatment of tender offers and proxy contests involving Commission licensees or companies with controlling interests in Commission licensees." Tender Offers and Proxy Contests, supra, 59 RR 2d at 1584.

12. The Commission's design and adoption of a bifurcated procedure for use in connection with tender offers involving publicly traded corporations which either hold licenses issued by the Commission or have controlling interests in such corporations were governed by four principal objectives: (1) to further the broad statutory mandate and comply fully with the procedural requirements of the Communications Act; (2) to act expeditiously and avoid unnecessary delay, because delay often favors one party in the contest for control; (3) to use procedures which promote strict governmental neutrality, favoring neither incumbents nor challengers; and (4) to accommodate to the fullest extent possible state and other federal laws and policies concerning the governing of corporations. Tender Offers and Proxy Contests, supra, 59 RR 2d at 1539-40. The Commission found that a two-step procedure met these objectives. Id. at 1583.

13. Mechanically, the first step of the bifurcated procedure entails the grant of an STA to a trustee to permit the collection and purchase of the tendered shares and to operate the licensed facilities, subject to specified conditions. In reviewing requests for special temporary authorizations in the context of tender offers, the Commission confines its examination to the trust instrument, the proposed trustee's qualifications and, if challenged, the offeror's ability to finance the tender offer. Macfadden Acquisition Corp., (Macfadden I), 104 FCC 2d 545, 565-66 (1986). If the tender offer is successful, the second step involves consideration of the offeror's qualifications under the formal procedure specified in Section 309(d) of the Communications Act.[12] In this case, § 78.35 of the Commission's Rules, 47 CFR

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[12] The Commission requires strict adherence to the requirements of Section 309(d) of the Communications Act in step two, including the formal opportunity for public comment, before an offeror will be permitted to assume control of a Commission licensee. As noted above, on March 14 and 16, 1994, Rogers filed six additional applications for transfer of control of various CARS licenses associated with Maclean's New Jersey cable system. Public notice of the acceptance for filing of those applications was provided on March 17, 1994. See Public Notice, Report No. 1152. Therefore, pursuant to Section 78.20(c) of the Commission's Rules, the requisite 30-day public comment period will not expire until April 18, 1994.

Pursuant to Section 310(d) of the Communications Act, grant of the step two applications is dependent upon a finding that the public interest, convenience

§ 78.35, also applies.[13] See e.g., Viacom Inc., 8 FCC Rcd 8439, 8440 (1993); QVC Network, Inc., supra, 8 FCC Rcd at 8486; CNCA Acquisition Corp., 3 FCC Rcd 6088, 6089 (1988); Macfadden Acquisition Corp. (Macfadden II), supra, 60 RR 2d at 873; JB Acquistion Corp. (Reliance I), 60 RR 2d 1095, 1098 (1986). Pending Commission action on the second step applications, the offeror is proscribed from exercising control over the tendered shares and from attempting to influence the actions of the trustee. If the Commission finds the offeror unqualified to be a Commission licensee, the trustee alone must dispose of the target company's stock, setting terms and conditions for that sale.

14. The two-step process invoked by Rogers has been used in the past by applicants seeking to acquire control of a company by tender offer. In CNCA Acquisition Corp., supra, 3 FCC Rcd at 6088, CNCA Acquisition Corp. ("CNCA"), sought to acquire control of American Cellular Network, Corp. ("AmCell"), by means of a hostile tender offer and filed applications with the Commission seeking to utilize the two-step procedure authorized in the Policy Statement. The Commission granted CNCA's request for an STA to permit the transfer of tendered shares of AmCell to a trustee, finding that a grant would serve the public interest, convenience and necessity. In Viacom Inc., supra, 8 FCC Rcd 8439 (1993) and Eugene McCarthy, 60 RR 2d 1207 (1986), the Commission granted STAs to permit the transfer of tendered shares to trustees pending review of long-form transfer of control applications in friendly tender offer circumstances. However, in both cases, there were concurrent competing hostile tender offers for the same companies, for which STAs were also granted to permit the transfer of the target companies' tendered shares to trustees. See QVC Network, Inc., supra, 8 FCC Rcd 8485; Macfadden Acquisition Corp., (Macfadden II), supra, 60 RR 2d 872. Thus, in these later four cases, similar and equitable treatment of the competing offerors was necessary in order to comply with the policy objective of strict governmental neutrality. Previously, in JB Acquisition Corp. (Reliance I), supra, 60 RR 2d at 1098, the Commission noted that the two-step procedure had been utilized to "permit attempts at hostile takeovers by tender offer, as a hostile tender offer by its nature requires prompt action. While the same procedure would not normally be necessary in the case of a friendly tender offer, it is apt where a competing offer already exists, so that the second offeror must be promptly empowered to present its offer to the shareholders."[14]

15. In an unpublished decision involving the friendly merger of Communications Industries, Inc. ("CI"), with Pacific Telesis ("PacTel"), the Common Carrier Bureau specifically held that while the particular circumstances of that transaction warranted expeditious handling, no

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and necessity will be served, including an analysis of the competitive impact, if any, of the proposed acquisition.

[13] Section 78.35 of the Commission's Rules provides, in relevant part, that no transfer of control of a CARS license shall occur without prior FCC authorization.

[14] See also MMM Holdings, Inc., 4 FCC Rcd 6838, n.1, aff'd. 4 FCC Rcd 8243 (1989)(the Commission "formalized [the two-step] procedure to grant a special temporary authorization to a trustee, pending consideration of a 'long-form' application, for hostile takeover cases . . .").

extraordinary circumstances existed which warranted use of an STA.[15] Communications Industries, Inc., CCB Memorandum Opinion and Order, released November 8, 1985, 1985 FCC LEXIS 2329, *21, n.13. Rather, the Bureau found that the proposed temporary transfer of CI's stock from its shareholders to a trustee did not involve a "substantial" transfer within the meaning of Section 309(c)(2)(B) of the Communications Act and granted the pro forma applications implementing the first phase of the transaction. Id. at *21.

16. The propriety of the use of the two-step procedure is not challenged in the instant case. However, the circumstances surrounding this case warrant discussion of the application of the two-step procedure.

APPLICATION OF THE TWO-STEP PROCEDURE

17. OVERVIEW. When the initial STA applications were filed with the Commission, Rogers' tender offer for Maclean was hostile.[16] At that point in the process, the STAs were clearly necessary to allow Rogers to acquire tendered shares pending Commission review of applications for transfer of control of Maclean. See, e.g., CNCA Acquisition Corp., supra, 3 FCC Rcd 6088. As Rogers argued in its STA request, implementation of the trust mechanism would assure that the tender offer received fair consideration by Maclean's shareholders and that Maclean's shareholders retained their right to make effective choices as to the management of their company. STA Request, Overview at 10-11. It would also prevent Maclean from using Commission procedures to block or delay the tender offer or insulate its management from the rigors of the marketplace. STA Request, Attachment at 1. Moreover, Rogers asserted that the "Commission adopted the two-step procedure . . . in order to provide a framework for the neutral regulatory treatment of such hostile tender offers," and that grant of the STAs would assure Commission neutrality and noninterference in connection with this proposed transaction involving two Canadian companies. STA Request at 2 and Attachment at 1-2.

18. While the STA requests were still pending before the Commission, the parties negotiated a cooperative agreement.[17] And, as noted above, Maclean's board of directors issued a revised Directors' Circular approving the agreement and unanimously recommending that shareholders accept Rogers' amended tender offer. On March 11, 1994, Rogers requested that the Commission

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[15] The Bureau stated that:

> [A]dministrative delay will not prevent consideration of the tender offer at an impending shareholders meeting. In addition, this is not a situation where administrative delay will aid incumbent management in frustrating a hostile tender offer by repurchasing the company's own securities or announcing dividend increases or stock splits. Id.

[16] As noted above, Rogers' February 14, 1994, tender offer was formally opposed by the Maclean board of directors on February 23, 1994. See Rogers' March 14, 1994, submission of Maclean's Directors' Circular.

[17] The March 8, 1994, letter agreement was submitted to the Commission as Annex C to Rogers' March 11, 1994, Request For Continued Use of Special Temporary Authorization in Light of a Recent Conditional Agreement.

continue to process the STA requests in accordance with the two-step procedures announced in the Commission's Policy Statement.[18] Maclean supports Rogers' request for continued application of the two-step procedures.[19] Rogers' applications are unopposed.[20]

19. THE POLICY STATEMENT. To determine whether the two-step procedures are appropriate in this case, our analysis must first consider whether a grant of an STA in the circumstance presented here -- that is, a hostile tender offer is accepted by the target company while the STA request is pending before the Commission -- would be consistent with the Policy Statement.

20. *The parties' contentions.* Rogers asserts that the Policy Statement provides for the use of a trustee and two-step procedures in all tender offer situations. Request at 9. In support of its contention that the Commission did not intend to limit the availability of an STA to hostile tender offers, Rogers cites to two sentences in the Policy Statement (Id.):

> [W]e find that Section 309(f) empowers us to grant an STA to a trustee in all situations involving a tender offer of a communications company.

(Tender Offers and Proxy Contests, supra, 59 RR 2d at 1569 n. 147) and

> Because the policies adopted in this proceeding must accommodate situations in which the offeror is hostile to current management as well [sic] those in which no such hostility exists, we believe that the trustee requires a certain degree of flexibility in the manner in which he or she exercises control over the corporation.

Id., 59 RR 2d at 1581. Maclean asserts that the Policy Statement, on its face, does not limit the availability of the two-step procedures to tender offers that remain hostile until Commission grant of an STA. Maclean letter filing at 3.

21. Rogers and Maclean both argue that denial of two-step procedures in the situation presented here would create an anomalous and undesirable result in terms of the Commission's goals of expedition and maintenance of neutrality in tender offer cases. For instance, the parties assert that if the STA mechanism is not available when a target company provides conditional support to a tender offer, such support could jeopardize prompt closing of the

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[18] See Rogers' March 11, 1994, Request for Use of Special Temporary Authorization in Light of a Recent Conditional Agreement.

[19] See Maclean's March 17, 1994, letter filing.

[20] An informal objection to the proposed transfer to Rogers, addressed to President Clinton from Mr. Stanley Y.T. Wan, was forwarded to the Commission. The informal objection was not properly filed with the Commission and addresses the step two transfer applications, thus is not considered herein. By this action, however, we are not precluded from considering the informal objection in connection with the step two applications.

offer or could be used as a defensive measure to prevent prompt closing. Request at 6-7; Maclean letter at 3. Maclean also argues that discouraging the target from settling differences with an offeror could provide the parties an incentive to collude in maintaining the appearance of a continuing hostile transaction in order to circumvent the Commission's rules. Maclean letter at 3.

22. *Discussion.* We believe the salient point of our analysis should be the status of the tender offer at the time the STA request was filed and public notice issued. In this case, Rogers' tender offer demonstrably was a *bona fide* hostile tender offer at the time the initial STA requests were filed with the Commission.[21] The Commission has determined that the two-step procedure, including the trust mechanism, is available to companies seeking to acquire a company holding Commission licenses through a hostile tender offer. To ascertain the impact of the subsequent change of position by the target on the continued availability of the two-step procedures, we must examine whether such procedures are consistent with the crucial objective underlying the Policy Statement of full compliance with the procedural requirements of the Communications Act.

23. In adopting the Policy Statement, the Commission found that the mandatory application of traditional transfer of control procedures in tender offer situations disserved the public interest because the delays inherent in such procedures deterred companies from utilizing the legitimate vehicle of tender offers in take-over bids for companies holding Commission licenses. Denying an STA because the target of a hostile tender offer reverses its opposition to the tender offer prior to Commission action on pending STA requests would add a level of uncertainty and delay to the transaction which could similarly deter companies from utilizing the tender offer process.[22]

24. Additionally, making the availability of the two-step procedure contingent upon continued hostility would be inconsistent with the Commission's objective of ensuring its regulatory procedures are neutral. A denial of an STA request filed when the transaction was a *bona fide* hostile tender offer could lead to the anomalous result that by negotiating an acceptable offer early in the tender offer process, the target company's board of directors would affect a significant delay in consummation of the tender offer. As noted in the Policy Statement, such delays in the context of tender

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[21] The background and history of the proposed transaction, as delineated in Rogers' SEC Form F-8 demonstrates arms-length negotiations, adversarial regulatory agency and court battles, oppositional press releases, and other indices of hostility between the parties. Maclean's Directors Circular delineates similar indices of hostility and expressly urges its shareholder not to tender shares to Rogers.

[22] To avoid loss of valuable time if the transaction should turn friendly pending Commission action on STA requests, parties in the future may be tempted to file not only the applications required pursuant to the two-step procedures, but also a contingent "long form" application for transfer of control to a trustee. However, our rules prohibit the filing of conflicting or inconsistent applications. Thus, an anomalous situation would be created by denying a STA in the situation presented here where the two-step applications were filed in connection with a *bona fide* hostile tender offer.

offers disserve the public interest. Tender Offers and Proxy Contests, supra, 59 RR 2d at 1557-62. Moreover, denial of an STA in a situation such as presented here could create an untenable Catch-22 for the board of directors of a target company that determined early in the process to support the tender offer: in order to ensure timely consummation of the transaction, the board would need to stall or delay cooperation, collude with the offeror or oppose the offer pending receipt from the Commission of the STA.[23]

25. We find that the rationale supporting the Commission determination that the two-step procedure, including the trust mechanism, is available to companies seeking to acquire a company holding Commission licenses through a hostile tender offer, is equally applicable to the situation presented in this case, where at the time the STA request is filed with the Commission, the transaction is a *bona fide* hostile tender offer.

26. APPLICATION OF THE POLICY STATEMENT TO THE FACTS OF THIS CASE. We now turn our analysis to whether the specific circumstances of this case warrant application of the two-step procedures and whether such application is consistent with the Policy Statement and the Commission's objectives of maintaining neutrality between companies engaged in take-overs, avoiding unnecessary regulatory delay, and accommodating other federal laws concerning the governing of corporations.

27. *The parties' contentions.* Rogers asserts that the letter agreement of March 8, 1994, and subsequent revised tender offer reflect a conditional accommodation and not a typical friendly merger.[24] According to Rogers, the tenuous and atypical nature of this transaction is exemplified by Maclean's imposition of conditions upon its agreement to recommend the tender offer to its shareholders. Rogers asserts that Maclean imposed tight time requirements on Rogers' ability to take up and pay for Maclean shares, such that if the contractual deadlines specified in the letter agreement are not met, the transaction may once again become a hostile situation.[25] Moreover, Rogers argues that its ability to consummate the tender offer will be severely impeded if it is unable to take up shares on or prior to March 31, 1994, because shareholders would then be permitted under Canadian securities laws to withdraw their tendered shares after that date. Rogers also asserts that if the Commission precluded use of the trustee mechanism, Maclean's shareholders

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[23] The overriding fiduciary obligation of a target companies' board of directors to act in the best interests of the shareholders of the company should prevent a target company from opposing an offeror's tender offer merely to take advantage of the trust mechanism. This same obligation should preclude manipulation of transactions in order to take advantage of Commission policies.

[24] See Rogers' March 11, 1994, Request For Continued Use of Special Temporary Authorization in Light of a Recent Conditional Agreement, at 4-6. Rogers' March 11, 1994, Notice of Extension and Variation of Offer to Purchase Common Shares was submitted to the Commission on March 14, 1994.

[25] In addition to the requirement for expeditious consummation of the tender offer, Maclean reserved termination rights, rights to change its recommendations to its shareholders and rights to consider unsolicited third party offers during the pendency of Rogers' tender offer.

would be deprived of their ability to consider the current tender offer and receive the benefits of the transaction negotiated and recommended by Maclean's board. Request at 5, 10.

28. Maclean concurs in Rogers' assessment that the tender offer is not now "friendly." Maclean states that the directors determined that the revised tender offer was the best alternative among the opportunities available at the time the directors considered the revised tender offer, but that their agreement to support the revised tender offer was conditioned upon the expeditious consummation of the offer, which would be possible only through application of the Commission's two-step tender offer procedures. Maclean letter at 2.

29. Rogers asserts that the involvement of the Canadian layer of regulatory requirements presents circumstances that justify continued application of the Policy Statement's bifurcated procedures. Rogers argues that the Commission should attempt to accommodate the jurisdiction of the CRTC and the Ontario Securities Commission according to basic principals of comity.

30. Rogers also claims that because the tender offer was hostile at the time the STA request was filed and the Commission's public notice was issued, other regulatory authorities, including the CRTC and U.S. municipal and state franchise authorities, have relied and are continuing to rely on the trustee mechanism. Therefore, Rogers argues that regulatory consistency requires continued application of the two-step procedures.

31. *Discussion*. When the initial STA requests in this case were filed with the Commission, Rogers' tender offer was a *bona fide* hostile tender offer. The original tender offer was open for acceptance until March 15, 1994, and Rogers' retained sole discretion to extend the expiration date. The revised tender offer supported by Maclean, extends the acceptance date only 15 days, until March 31, 1994. As noted above, pursuant to Canadian securities regulations, any tendered shares not taken up and paid for may be withdrawn by the tendering shareholders after March 31, 1994. Further, under the terms of the revised offer, if Rogers' fails to take up and pay for all tendered shares by April 30, 1994, Maclean's obligations under the March 8, 1994, agreement terminate and Maclean is free to withdraw support for the offer.[26]

32. Absent access to the trustee mechanism, the Commission's public notice and comment requirements would preclude Rogers from taking up and paying for the tendered shares of Maclean by March 31, 1994.[27] If a single

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[26] Pursuant to Canadian securities regulations, shareholders remain free to withdraw tendered shares which are not taken up and paid for by Rogers throughout the one month extension period.

[27] As noted above, on March 14 and 16, 1994, Rogers filed six additional applications for transfer of control of various CARS licenses associated with Maclean's New Jersey cable system. Public notice of the acceptance for filing of those applications was provided on March 17, 1994. See Public Notice, Report No. 1152. Therefore, pursuant to Section 78.20(c) of the Commission's Rules, the requisite 30-day public comment period will not expire until April 18, 1994. (We note that the STA requests filed on March 16, 1994, were returned by the fee processing branch and refiled on March 25,

opposition to the transfer is filed, whether by a dissenting director, a franchise authority, a consumer group or a shareholder of either company, Rogers would be also precluded from taking up and paying for the tendered shares of Maclean by the extension date of April 30, 1994.[28] On that date, if the tendered shares are not taken up and paid for by Rogers, the period of cooperation agreed upon by the parties in their March 8, 1994, agreement expires and Maclean may terminate the transaction.

33. We are persuaded that absent access to the trustee mechanism, the Commission's public notice and comment procedures could effectively preclude Maclean shareholders from exercising their rights to tender shares to Rogers under the current tender offer. Regulatory delay which adversely affects one party or which affects shareholder rights disserves the public interest. Tender Offers and Proxy Contests, supra, 59 RR 2d at 1558-62.

34. We are also persuaded that the agreement the parties entered into on March 8, 1994, and Maclean's acceptance of Rogers' revised tender offer is sufficiently time sensitive and conditional that failure to grant an STA here could act to interfere with the normal course of the tender offer process. Such action would be inconsistent with the objective of the Policy Statement of ensuring procedures which maintain neutrality between parties engaged in take-over situations. We note that the parties have expressly conditioned their continued cooperation on expeditious action and tied their contractual timelines to relevant Canadian securities regulations. Therefore, we find that expeditious action here would be consistent with the Policy Statement.

35. Additionally, we note that in tender offer situations the CRTC permits tendered shares to be held by a trustee pending its review of a transfer of control of Canadian issued licenses,[29] and with respect to this transaction, the CRTC has approved the nomination of Pierre Juneau as trustee. If we also grant the requested STAs, procedures within both countries will be parallel. This would be consistent with the Policy Statement objective of ensuring our procedures are neutral and do not affect the transaction.[30]

1994. Because public notice of the STA requests had previously been released, no additional public notice was issued by the Bureau.)

[28] Pursuant to Sections 1.4, 1.45 and 78.22 of the Commission's Rules, if petitions to deny the applications are filed, the pleading cycle in this case would last until at least May 12, 1994.

[29] See, e.g., transfer of effective control of Greater Winnipeg Cablevision (Decision CRTC 87-890) which involved the transfer of the shares held by Selkirk Communications Limited to a trustee pending CRTC approval of the transaction; transfer of control of Standard Broadcasting to Slaight Broadcasting (Decision CRTC 85-1146) which involved the holding of a proxy for the voting shares pending CRTC approval; transfer of effective control of Multilingual Television to Rogers Broadcasting Limited (Decision CRTC 85-586) which involved the holding of a proxy.

[30] However, were we to deny the requested STA, in order for Rogers to then be able to utilize the trustee mechanism before the CRTC, an application for transfer to Juneau would need to first be approved by the Commission, followed by an application to transfer to Rogers. As noted above, the attendant delays of traditional transfer procedures would likely adversely

36. Numerous Canadian and United States regulatory bodies are involved in this transaction. Of particular importance to our analysis is the Multijurisdictional Disclosure System between the United States and Canada ("MJDS").[31] Pursuant to the MJDS, Canadian issuers meeting prescribed eligibility requirements may satisfy securities registrations and reporting requirements of the SEC by providing disclosure documents prepared in accordance with the requirements of Canadian securities regulatory authorities. The MJDS also allows certain cash tender and exchange offers for securities of Canadian issuers to proceed in accordance with Canadian and provincial or territorial tender offer requirements instead of in accordance with SEC tender offer requirements. The MJDS and the SEC's implementing regulations are intended to facilitate cross-border offerings of securities and continuous reporting by specified Canadian issuers and to remove unnecessary impediments to transnational capital formation.

37. While neither transnational nor cross-border securities nor the particular securities policies and regulations involved here have been addressed in prior Commission tender offer cases, our consideration of the federal policies embodied in the SEC regulations implementing the MJDS is consistent with yet another of the Commission's stated policy goals in designing the two-step procedures: to accommodate to the fullest extent possible the diverse state and federal laws and policies governing corporations. Tender Offers and Proxy Contests, supra, 59 RR 2d at 1554. In addition, in other contexts, particularly in the area of frequency coordination, the Commission has endeavored to cooperate with Canada.[32]

38. Finally, with respect to regulatory approvals from U.S. state and municipal franchising authorities, we note that our action here on the STA request does not preempt any U.S. state or municipal franchising authority action. See CNCA Acquisition Corp., supra, 3 FCC Rcd at 6090; L.P. Media, Inc., supra, 102 FCC 2d at 1278; see also King Kable, Inc., 8 FCC Rcd 1515, 1516 (1993)(FCC waiver of three-year holding period in transfer of cable system made expressly contingent upon franchising authority approval); Tender Offers and Proxy Contests, supra, 59 RR 2d at 1560 (the Commission is "not charged with overseeing the entire tender offer process and delays not attributable to [FCC] procedures are beyond the scope of [the FCC's] regulatory concern").

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impact the timely consummation of the tender offer and could jeopardize the deal.

[31] Securities and Exchange Commission Release No. 34-29354, 56 Fed. Reg. 30,036 (July 1, 1991); see 17 CFR § 240.14d-1(b); see also 17 CFR § 239.38(SEC Form F-8 used to register certain Canadian securities to be issued as part of an exchange offer).

[32] See e.g., U.S. and Canada Announce Private Land Mobile Cross-Border Agreement, 1991 FCC LEXIS (April 30, 1991); Commission and Canadian Department of Communications Agree on Interim Channeling Arrangement for the 136-137 MHz Aeronautical Mobile (R) Service Band, 7 FCC Rcd 1802 (1992); Amendment of Part 74 of the Commission's Rules Regarding FM Booster Stations, 6 FCC Rcd 6060, n.2 (1991).

39. Based upon the particular circumstances presented here we find that use of the two-step procedure is appropriate and will further the Commission's tender offer policy objectives of achieving full compliance with the mandates of the Communications Act, ensuring neutrality, avoiding unnecessary delay and accommodating to the fullest extent possible, other federal laws and policies. The facts we find determinative are that: (1) the take-over transaction began as a hostile tender offer and was still hostile when the initial STA requests were filed with the Commission and when the Commission issued a public notice announcing the filing of the STA requests; (2) notwithstanding a cooperative agreement, the parties' continued cooperation is contingent upon prompt consummation of the tender offer; (3) U.S. securities policies, through SEC regulations implementing the terms of the MJDS, endeavor to facilitate such transnational transactions and cross-border offerings as are involved here; (4) Canadian securities regulations, compared with U.S. securities regulations, constrict the time an offer can remain open before shareholders are permitted to withdraw tendered shares, and thus add complicating time exigencies to the transaction; and (5) both companies involved are Canadian and a majority of the assets to be acquired are Canadian, although a substantial portion are located in the U.S.

ROGERS' TRUST INSTRUMENT

40. Our review of the step-one applications includes examination of the trust instrument to ensure that the offeror is restricted from exercising direct or indirect control over the licensee from the time the tender offer is consummated until all requisite regulatory approvals are obtained, the trustee is effectively insulated from an offeror's influence, and the trustee's obligation as a temporary caretaker charged with preserving the nature and character of the corporation is properly delineated. Tender Offers and Proxy Contests, supra, 59 RR 2d at 1578-81. According to the terms of the Amended and Restated Voting Trust Agreement executed by Rogers and its designated trustee, Pierre Juneau, all shares acquired by Rogers in its tender offer, and all shares or equity interests then owned by Rogers, will be simultaneously transferred and delivered to the trustee [33] Trust Agreement at § 1. The trust arrangement will commence upon Rogers' taking up and paying for the Maclean shares tendered under the tender offer, following FCC consent to the STA. Trust Agreement at § 7. During Commission review of Rogers' step two applications, all voting rights of the Rogers-held shares will be vested in and exercised by the trustee, while Rogers will own the equitable interest in those shares, entitling it to receive dividends, interest and other distributions (other than Maclean voting securities).[34] Trust Agreement at p.

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[33] The Amended and Restated Voting Trust Agreement between Rogers and Pierre Juneau, P.C., O.C., dated March 24, 1994, (hereinafter "Trust Agreement"), submitted to the Commission on March 25, 1994, expressly supersedes and replaces in all respects the Voting Trust Agreement entered into by the parties on February 28, 1994, and submitted to the Commission as Attachment C to the STA requests.

[34] Section 2(c) of the trust instrument provides that the trustee shall grant security interests in the deposited shares to secure loans to enable Rogers to acquire all or part of the deposited shares. A similar provision was approved in Viacom, Inc., supra, 8 FCC Rcd at 8441 n. 12. Consistent with Commission policy as set forth in Attribution of Minority

2 and §§ 2(c), 4(a), 4(b) and 6. The trustee must exercise its voting rights in a manner to effectuate and implement Rogers' tender offer, carry on the business of Maclean in the ordinary course, and safeguard the assets and maintain the continuity of the operations and general character of Maclean consistent with facilitating the tender offer. Trust Agreement at § 4.

41. The trust instrument does not contemplate the trustee serving as a director of Maclean. Rather, the trust instrument provides the trustee absolute discretion to vote the Rogers-held shares to continue the current board of directors of Maclean. Trust Agreement at § 4(a)(iii). The trust instrument also provides the trustee with the right to vote the Rogers-held shares to require a shareholders meeting to be held to remove any director of Maclean from office by ordinary resolution for cause, i.e., for opposing, impeding or impairing the effectuation of the tender offer, or failing to render all assistance necessary to effectuate the tender offer, or wasting corporate assets, or failing to act in a manner so as to maintain the continuity of the operations and general character of Maclean and its subsidiaries in the ordinary course of their respective businesses, or otherwise acting in a manner inconsistent with such director's fiduciary responsibilities, or failing to act in accordance with the policies and guidelines set forth in the Policy Statement. Trust Agreement at § 4(a)(i).

42. With regard to the ability to require a shareholders meeting to remove directors, the trustee may not elect or appoint a majority of the board of directors at the time that Rogers takes up and pays for the tendered shares; however, the trustee maintains the ability during the term of the trust to replace any member of the board of directors who resigns or is removed for cause. Trust Agreement at § 4(a)(ii). A replacement director must bear a relationship to Rogers as strict as that of the trustee to Rogers, i.e., having no professional, business or familial relationship with Rogers or any partner, officer, employee, director, shareholder, or affiliate of Rogers. Trust Agreement at § 4(a)(ii). Permitted communications between the trustee and Rogers are restricted to one-way written communications from the trustee to Rogers concerning the management and operations of Maclean and two-way written communications to and from Rogers concerning the mechanics of implementing the tender offer. Trust Agreement at § 8. However, the trust instrument does not specify that these same communications restrictions apply to directors nominated or appointed by the trustee. Consequently, we are imposing these restrictions as a condition of the STA.[35]

Ownership, 99 FCC Rcd 1249, 1254 (1985), the Trust Agreement expressly provides for the inclusion of three conditions in any security agreement involving a pledge of Rogers' stock: (1) the voting rights for any pledged stock will remain with the trustee, even in the event of default on the loans; (2) in the event of a default, there will be a public or private sale of the stock; and (3) prior to the exercise of stockholder rights by a purchaser at such price, the prior consent of the Commission will be obtained.

[35] Any person appointed or nominated by the trustee, and elected, to the board of directors shall be subject to the same restrictions and conditions on communications applicable to the trustee, that is, communications to the offeror relating to the tender and purchase of shares or to the maintenance and operation of the target company must be in writing, no

43. The rights and duties of the trustee, who is to be compensated by Rogers for his services, terminate upon his bankruptcy, insolvency or death. Trust Agreement at §§ 5(b) and 5(e). If such circumstances occur, or the trustee resigns by giving Rogers 60 days' advance written notice, he will be succeeded, subject to such prior CRTC and FCC consent as may be required, by a successor trustee chosen by Rogers. Trust Agreement at §§ 5(f) and 5(h).

44. The trust instrument is expressly irrevocable until all requisite consents of the FCC, the CRTC and local U.S. authorities to the applications for transfer of Maclean to Rogers are obtained and all the deposited shares are transferred to Rogers, or if the necessary consents are not obtained, until completion of the sale of all the deposited shares or other assets of Maclean. Trust Agreement at §§ 1(a), 1(b), 4(c), 4(d) and 7. In the latter situation, if Rogers notifies the trustee that the requisite consents have not been obtained, the trustee has discretion to determine the sale procedure, select the purchasing party or parties and determine the terms of the sale with a view to obtaining the best value reasonably obtainable; provided that Rogers may withdraw a request for sale at any time prior to consummation, subject to the independent concurrence of the trustee. Trust Agreement at § 4(d). The trust instrument further provides that upon receipt of all requisite consents, including prior Commission consent, the trustee shall dispose of assets that do not utilize any Commission license in a manner consistent with written requests from Rogers.[36] Trust Agreement at § 4(e). Finally, the trust instrument may only be amended following receipt of necessary approvals of the Commission or the CRTC. Trust Agreement at § 9(b).

45. No provision of the Rogers trust instrument is challenged. After reviewing the Trust Agreement, we conclude that the trust instrument ensures that Rogers will be restricted from exercising control during the term of the trust, the trustee will be properly insulated and independent from Rogers, and the trustee will be obligated to safeguard Maclean's assets, assure continuity of operations and facilitate the consummation of the tender offer. We also find that the terms of the trust instrument are consistent with Commission case precedent and that the trust instrument complies with Commission policy governing trusts in tender offer cases.

ROGERS' TRUSTEE

46. As noted above, our review of STA requests in tender offer cases includes examination of the qualifications of the trustee. Rogers' designated trustee, Pierre Juneau, P.C., O.C., is a Canadian citizen and a former

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communications shall be made by the offeror, orally or in writing, relating to the management or operation of the target company, and communications from the offeror in connection with the tender and purchase of shares must be in writing.

[36] In Macfadden Acquisition Corp. (Macfadden I), 104 FCC 2d 545, 563 (1986), the Commission tacitly approved a provision in a trust instrument permitting the sale of nonbroadcast assets of the target company by the trustee pending Commission action on the step-two application. Because the provision in this case requires prior FCC approval of any disposition of assets not involving Commission licenses, we believe the provision is consistent with extant case precedent.

President and Chief Executive Officer of the Canadian Broadcasting Corporation, Deputy Minister of Communications, Under Secretary of State, Chairman of the National Capital Commission, Minister of Communications and Chairman of the Canadian Radio Television Commission. He currently is a visiting professor at the University of Montreal and Chairman of the Canada Center for International Study and Cooperation. According to the FCC Form 327, he is not a representative of a foreign government.[37] According to the STA request, he has no familial or business relationship direct or indirect except for the Voting Trust Agreement, to Rogers, Rogers' affiliates, Maclean, Maclean's affiliates, and their respective officers, directors or principals. He has no cognizable interest in any media or telephone properties that would, upon commencement of the trust, cause a violation of the Commission's ownership rules. He has not been found by any court or administrative body to have committed any felony, criminal fraud, or fraud or misrepresentation before a governmental unit, or any action in violation of any antitrust, unfair competition, or nondiscrimination law or regulation, or any violation of the Communications Act or any Commission rule or policy. No party has questioned the qualifications of Juneau and we find him qualified to serve as trustee of Maclean on behalf of Rogers.

OTHER MATTERS

47. Applicants for CARS licenses are not required to certify financial qualifications, either in initial applications or in transfer or assignment applications. In the context of STA requests in tender offer cases, the Commission defers examination of the offeror's qualifications to be a Commission licensee until review of the step two applications for transfer of control to the offeror, confining consideration at the first step to the trust instrument, the trustee's legal qualifications, and, if challenged, the offeror's ability to finance the tender offer. See Viacom, Inc., supra, 8 FCC Rcd at 8440. No party has challenged Rogers' financial qualifications. Consequently, no financial qualification examination is required.

48. According to the STA request, all of Maclean's United States cable systems were acquired by Maclean more than three years ago. Consequently, were examination of the statutory anti-trafficking provision of Section 617 of the Communications Act, 47 U.S.C. § 537, appropriate during review of the first step applications, Rogers' applications would pose no conflict requiring resolution.

49. Rogers' stated intent to divest Maclean's U.S. cable systems in the event its tender offer is successful does not preclude invocation of the STA mechanism. See QVC Network, Inc., supra, 8 FCC Rcd at 8487. Additionally, because the Trust Agreement does not contemplate the sale of the U.S. cable businesses during the pendency of the trust arrangement, no concerns regarding the trustee's obligations to maintain Maclean's assets are raised. See Rogers' March 11, 1994, Notice of Extension and Variation of Offer

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[37] CARS licenses are governed by Section 310(a) of the Communications Act which provides that station licenses shall not be granted to or held by any foreign government or representative thereof. Consequently, no alien ownership issue is presented by Rogers' applications.

to Purchase, at 5.

CONCLUSION

50. We have reviewed the STA applications and conclude that grant of Rogers' request for an STA would serve the public interest, convenience and necessity.

Accordingly, IT IS ORDERED, That the request for special temporary authorization IS GRANTED to Pierre Juneau, Trustee, for 180 days from the release date of this decision, to solicit, collect and acquire the stock of Maclean Hunter Limited, subject to the representations set forth in its applications and pleadings, the conditions set forth in the Voting Trust Agreement, as amended, except as limited by this decision or the following conditions, which take effect upon the release of this Order, unless otherwise specified:

1. Rogers Communications Inc., its affiliates and the officers and directors of those corporations (collectively, referred to as Rogers) while the trust is in effect, shall not nominate a member of the board of directors of Maclean or its subsidiaries as their representative or influence the trustee's selection of directors. Any person appointed or nominated by the trustee, and elected, for the board of directors of Maclean shall be subject to the same restrictions and conditions applicable to the trustee, including restrictions and conditions on communications to and with Rogers, and shall have no familial ties or business relationships with Rogers. Any person appointed by the trustee as proxy shall be subject to the same restrictions and conditions applicable to the trustee, including restrictions and conditions on communications to and with Rogers, and shall have no familial ties or business relationships with Rogers.

2. The Rogers interests will not involve themselves, directly or indirectly, in the operation or management of Maclean, or seek to influence the operation or management of Maclean.

3. Any communications from the trustee to Rogers relating to the tender and purchase of shares from the present shareholders or to the maintenance and operation of Maclean must be in writing. No communications shall be made by Rogers to the trustee orally or in writing, relating to the management or operation of Maclean. Communications from Rogers to the trustee in connection with the tender and purchase of shares must be in writing.

4. The trustee will maintain the status quo, as defined in Tender Offers and Proxy Contests, 59 RR 2d 1536 (1986). This directive requires that the trustee act so as to maintain the present management and operations of Maclean. The trustee will have the discretion to oppose only actions inconsistent with the preservation of corporate assets or actions that would be inconsistent with the transfer of control, if approved, to Rogers.

5. Rogers may direct the trustee to pledge the acquired stock only for purposes of securing a loan whose proceeds will be utilized in consummating the tender offer, provided that any security agreement entered into by the trustee includes the following provisions: (a) the voting rights for any pledged stock remains with the trustee, even in the event of a default by Rogers on the loans; (2) in the event of a default, there will be a public or private sale of the stock; and (3) prior to the exercise of shareholder rights by the purchaser at such sale, the prior consent of the Commission is obtained.

6. There shall be no substantial changes in the Voting Trust Agreement, as amended, except as may be necessary to comply with this Order, or as may be approved in advance by the Commission. Any insubstantial changes in that instrument must be filed promptly, within 10 days of the date of execution, with the Commission, with a copy to the Chief of the Competition Division of the Cable Services Bureau.

7. In the event that the applications to transfer control to Rogers are not approved, the trustee shall notify the Commission promptly, within 30 days after a final determination by the Commission or the CRTC, after a court-ordered sale, or after Rogers and the trustee jointly determine that such a transfer will not be pursued, with regard to the trustee's plans for disposing of the stock in the shortest period possible.

8. Any request for an extension of this authorization, if needed, shall be filed at least 30 days in advance of the expiration date.

The Cable Services Bureau will send copies of this Memorandum Opinion and Order to the parties to this proceeding by certified mail, return receipt requested.

CABLE SERVICES BUREAU

Alexandra M. Wilson

Alexandra M. Wilson
Acting Chief

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

FCC 93-341

In the Matter of Applications of	)	
	)	
Norris Satellite Communications, Inc.	)	File Nos. 54-DSS-P/L-90
	)	55-DSS-P-90
	)	
Application for authority to Construct, Launch and Operate Communications Satellites in the Ka-Band	)	

MEMORANDUM OPINION AND ORDER

Adopted: July 1, 1993 Released: July 20, 1993

By the Commission:

I. INTRODUCTION AND BACKGROUND

1. Norris Satellite Communications, Inc. (NorSat) has filed a Petition for Reconsideration of our Order and Authorization granting NorSat's applications to construct, launch and operate a domestic fixed-satellite (NorStar I) in the 20/30 GHz frequency bands (Ka-band).[1] We received a late filed opposition from Motorola Satellite Communication, Inc. (Motorola).[2]

2. Specifically, NorSat requests that the Commission revise the NorSat Order to permit the construction of two and operation of one satellite in the 19.5-20.2 GHz[3] and 29.3-30.0 GHz[4] bands. In the NorSat Order, we authorized use of the 19.7-20.2 GHz and 29.5-30.0 GHz receive and transmit frequency bands, respectively. Norris claims it asked for and should have received authority to operate in a total 1,400 MHz bandwidth assignment, not the 1000 MHz bandwidth assignment approved.[5]

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1 Norris Satellite Communications, Inc., 7 FCC Rcd 4289 (1992) (NorSat Order). In this Order and Authorization we also granted NorSat authority to construct another domestic satellite (NorStar II) to be held in reserve as an on-ground spare.

2 In its opposition, Motorola raised several technical and legal objections that have become moot in light of our disposition of Norris's reconsideration request.

3 This represents the receive or space-to-Earth frequency band.

4 This represents the transmit or Earth-to-space frequency band.

5 To support its claim, NorSat asserts that it stated in its application that its satellites were designed to operate using 1,400 MHz of bandwidth. Also, the total bandwidth assignment is the sum of both the receive and transmit bandwidth assignments.

II. DISCUSSION

3. In 1991, Harris Corporation and Suite 12 Group filed petitions for rulemaking[6] that formed the genesis of a Notice of Proposed Rulemaking (NPRM) to redesignate the 27.5-29.5 GHz frequency band and establish rules and policies for a local multipoint distribution service (LMDS).[7] In that NPRM, the Commission recognized that there may be conflicts between fixed-satellite services and terrestrial LMDS in that frequency band. Consequently, the Commission sought comment on developing appropriate spectrum sharing criteria between the co-primary services.[8] Also, the Commission urged commenters to "consider whether technical rules should be adopted to accommodate existing and proposed satellite use of the band."[9]

4. First, we note that NorSat, in its application, did not specifically request or justify use of a 1400 MHz bandwidth frequency assignment. Second, the operation of domestic fixed-satellites in the 29.3-29.5 GHz band may conflict with the terrestrial usage proposed in the NPRM. Thus, the Bureau's decision to limit NorSat to a 1000 MHz bandwidth assignment was correct. In addition, granting NorSat's petition at this time could prejudge the LMDS rulemaking before adequate comment has been received and analyzed. Further, we believe that an NPRM is a better forum for resolving spectrum sharing issues and therefore, we will not grant NorSat's petition. Our ability to entertain future fixed-satellite service applications will be determined by the outcome of the rulemaking proceeding.[10]

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6 Petition for Rulemaking filed by Harris Corporation (Farinon Division), RM 7722, Public Notice Report No. 1845, released May 15, 1991; Petition for Rulemaking filed by Suite 12 Group, RM 7872, Public Notice Report No. 21049, released December 16, 1991.

7 Rulemaking to Amend Part 1 and Part 21 of the Commission's Rules to Redesignate the 27.5-29.5 GHz Frequency Band and to Establish Rules and Policies for Local Multipoint Distribution Service, 58 Fed. Reg. 6400 (January 28, 1993) (NPRM).

8 See NPRM, note 6 supra, at para. 23.

9 Id., at para. 24.

10 With regard to NorSat's assertion that it should have received authority to operate using 1,400 MHz bandwidth, we conclude that NorSat did not clearly make that request. However, if NorSat had made a clear request, we would still have denied the request for the same reasons we deny the instant petition.

5. Accordingly, IT IS ORDERED that the Petition for Reconsideration filed by Norris Satellite Communications, Inc. IS DENIED for the reasons set forth above.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

FCC 94-32

In the Matter of	)	
	)	
Implementation of Section 309(j)	)	PP Docket 93-253
of the Communications Act	)	
Competitive Bidding	)	

FIRST REPORT AND ORDER

Adopted: February 3, 1994 Released: February 4, 1994

By the Commission:

1. The Omnibus Budget Reconciliation Act of 1993 ("Budget Act")[1] requires the Commission to prescribe rules that are necessary to prevent the unjust enrichment of recipients of licenses or permits that the Commission issues pursuant to the lottery authority granted by Section 309(i)(4)(C) of the Communications Act of 1934, as amended, 47 U.S.C. § 309(i)(4)(C) ("Communications Act"). This Report and Order responds to Congress' directive. We conclude that, in addition to the rigorous requirements that apply to lotteries in our existing rules, certain transfer disclosure rules are necessary to prevent unjust enrichment with respect to licenses issued by lottery. These requirements will enable us to monitor the operation and effect of lotteries closely over the next one to two years to enable us to determine if additional safeguards are necessary.

BACKGROUND

2. Our authority to issue licenses by lottery stems from Section 309(i) of the Communications Act of 1934, as amended, 47 U.S.C. § 309(i). In the Budget Act, Congress added a new statutory provision concerning unjust enrichment in the lottery context to this section of the Communications Act, which states that

> [n]ot later than 180 days after [August 10, 1993], the Commission shall prescribe such transfer disclosures and antitrafficking restrictions and payment schedules as are necessary to prevent the unjust enrichment of recipients of licenses or permits as a

[1] Pub. L. No. 103-66, title VI, § 6002(b)(1)(B), 107 Stat. 388, ___ (1993).

result of the methods employed to issue licenses under this subsection.[2]

3. In the Notice of Proposed Rule Making ("Notice" or "Auction Notice") implementing this and other sections of the Budget Act, we noted that the legislative history of this section indicated that the Commission might "impose or assess payments in order to prevent unjust enrichment resulting from trafficking in licenses."[3] We tentatively concluded that we could assess payments in order to prevent unjust enrichment from lotteries. We also asked for comment on what other antitrafficking restrictions were appropriate in addition to any payments we might impose. We suggested, for example, that we might place a three year restriction on the transfer of licenses gained through lotteries.

4. With respect to the term "unjust enrichment," it appears that Congress was concerned about transactions such as that mentioned in the Notice, where we observed that lottery winners of the rural cellular license for Columbia County, Wisconsin, sold it for $62.3 million in 1990, 165 days after a construction permit had been issued.[4] The legislative history of the Budget Act is highly critical of those who filed applications with no intention or capability of providing service but instead "only sought to acquire a license at nominal cost and then sell it, making a large profit and at the same time delaying the delivery of services to the public." House Report at 259. The legislative history reemphasizes the need for the Commission to limit "the ability of lottery winners to sell their license, so as to prevent the churning and profiteering that has characterized lotteries." Id.[5]

5. The Budget Act reduces significantly the Commission's authority to conduct lotteries. If the service or class of service is potentially eligible for competitive bidding under the statutory test in Section 309(j)(2)(A), then the Commission is precluded from using lotteries to resolve mutual exclusivity among applications. See 47 U.S.C. § 309(i)(1)(B). Because under the Budget Act certain mutually exclusive applications may still be resolved

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[2] 47 U.S.C. § 309(i)(4)(C).

[3] Implementation of Section 309(j) of the Communications Act, Competitive Bidding, PP Docket No. 93-253, 8 FCC Rcd 7635, 7649-50, para. 89 (1993), quoting H.R. Rep. No. 111, 103d Cong., 1st sess. 256 (1993) ("House Report").

[4] 8 FCC Rcd at 7641 n. 22. For purposes of this rule making and consistent with the intent of the Budget Act, "unjust enrichment" and "speculation" in the lottery context refer to the same act: the transfer of a license acquired by lottery for substantial profit prior to providing service to the public. Although the term "speculation" has also been associated with the large number of lottery applications generated by so-called application mills, we believe that the mere act of filing an application for a lottery does not give rise to the "unjust enrichment" that the Budget Act has required us to address.

[5] We note that this provision was adopted in conference from the House bill without change. See H.R. Rep. No. 213, 103d Cong., 1st sess. 489-90 (1993).

by a lottery, we sought comment in the Auction Notice on how to implement the subject statutory provision.

COMMENTS

6. Although we received approximately 300 timely filed comments and reply comments in this proceeding, we only received two comments and no reply comments that directly addressed the subject statutory provision. The Domestic Automation Company (DAC) stated that "bona fide entities who have lost in past lotteries often have had to buy [Multiple Address Service (MAS)] licenses from those who never intended to operate systems for their own use" and urged that we adopt strict rules and restrictions to stem speculation and trafficking in licenses won by lottery. Comments of Domestic Automation Company at 7. DAC also urged that the Commission adopt restrictions that would discourage potential traffickers from participating in Commission lotteries in the first place, such as a requirement for the posting of performance bonds, similar financial guarantees and annual spectrum user fees prior to the lottery. DAC also argues that we should adopt restrictions on licensees who either fail to construct or who construct and then quickly transfer their licenses, presumably for a profit. Id.

7. The American Petroleum Institute (API) shares these sentiments, noting that speculative interest in the radio spectrum has grown to the point where the Commission now is flooded with applications each time it announces an initial lottery for licenses. Comments of API at 7. Like Domestic Automation Company, API states that bona fide entities that lost in lotteries often have had to pay greenmail to speculators to obtain licenses they need, and urges the Commission to adopt strict rules and restrictions to stem speculation and trafficking in licenses won by lottery. Id. at 8.

DISCUSSION

8. The most egregious cases of unjust enrichment and speculation associated with past lotteries have occurred in "commercial" services,[6] where there are significant opportunities for the sale of licensed communications properties to third parties for profit. E.g., Cellular Radio Service. Therefore, possibly the strongest measure to deter future instances of unjust enrichment in the lottery context has already been taken by Congress when, in the Budget Act, it granted the Commission auction authority for all "commercial" spectrum-based services, and effectively took away the Commission's authority to conduct

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[6] See Auction Notice, 8 FCC Rcd at 7638-39 para. 25-28 (noting that for purposes of Section 309(j) of the Communications Act, "commercial service" means a subscriber-based service, and this term is substantively distinct from the term "Commercial Mobile Service," which is a term associated with Section 332 of the Communications Act).

lotteries for such commercial services.[7] Thus, under the Budget Act, any new rules adopted to implement the subject provision would potentially apply to only three classes of license applications: 1) mutually exclusive applications in certain private, internal-use services that meet the legislative criteria in Section 309(j)(2)(A) for random selection, but do not meet the legislative criteria for competitive bidding, 2) a limited number of mutually exclusive applications in commercial services accepted for filing prior to July 26, 1993, that the Commission has the authority to either auction or lottery under the Budget Act, and 3) possibly where a private, internal-use license application is mutually exclusive with a "commercial" use application for a license in "shared spectrum," that is, spectrum for which both entities are eligible to use.[8]

9. Furthermore, we note that the Commission has recently adopted rules that should assist in preventing unjust enrichment from lotteries in a variety of commercial services, including the Interactive Video and Data Service (IVDS), Multipoint Distribution Service (MDS) and Cellular Radio Service. These rules include, inter alia, transfer restrictions tied to an ascending scale of build-out requirements over the license term, anti-greenmail rules, settlement restrictions, and restrictions on changes in control of ownership. The Commission has not yet had the opportunity to fully evaluate the effectiveness of these rules because (1) the rules were adopted within the last two years (e.g., cellular radio[9] and MDS[10]), or the service is not yet operational (e.g., IVDS[11]).

10. Because in the future, only certain private, internal-use services would be

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[7] See Auction Notice, 8 FCC Rcd at 7637, para. 17 (noting that the Budget Act provides that the Commission may not issue any license or permit by lottery after the date of enactment unless the spectrum's use is not a type for which auctions are permitted, or the application was accepted for filing before July 26, 1993). Citing Section 6002(e) of the Budget Act (Special Rule). Under the Budget Act, therefore, mutually exclusive applications accepted for filing after July 26, 1993 may not be granted by lottery until the Commission determines whether the applicable radio service is not subject to competitive bidding under Section 309(j)(2)(A) of the Communications Act.

[8] See Auction Notice, 8 FCC Rcd 7658 paras. 139-140.

[9] See, e.g., Third Report and Order, Memorandum Opinion and Order, and Recon., CC Docket 90-6, 7 FCC Rcd 7813 (1992)(adopting, inter alia, anti-greenmail rules), and Report and Order, CC Docket 90-358, 7 FCC Rcd 719 (1992) (adopting anti-speculation rules in the context for comparative renewal proceedings).

[10] See, e.g., Amendment of Parts 1, 2 and 21 of the Commission's Rules in the 2.1 and 2.5 GHz bands, PR Docket 92-80, 8 FCC Rcd 1444 (1993)(adopting a variety of rules to deter unjust enrichment in the MDS context).

[11] See 47 C.F.R. Part 95, Subpart F.

subject to lottery, and such services rarely involve speculation or mutually exclusive applications, there does not appear to be a significant need at this time for new lottery rules to deter unjust enrichment. With respect to the limited number of "commercial" service applications that may be lotteried, the Commission has recently adopted rules in such services to deter unjust enrichment based on extensive experience in conducting lotteries in these services.[12] Before adopting additional measures, we believe it would be appropriate to gain some experience in how well these existing rules operate in practice.

11. In addition, the record compiled in this proceeding does not support adopting major additional measures to combat unjust enrichment in the lottery context. The two commenters that did address this matter focused primarily on MAS. In MAS, however, a licensee is required to meet certain construction benchmarks before it can transfer a license.[13] Therefore, while an MAS lottery may attract a large number of applicants, the existing construction benchmarks deter unjust enrichment by preventing licensees from transferring an MAS license before it provides service to the public.[14]

12. Further, the imposition of additional, more stringent restrictions could have adverse consequences. Because the randomly selected winner of a license may not value it the most highly, additional transfer restrictions could operate to deprive the public of valuable new communications services, reduce economic growth and limit the expansion of jobs. Therefore, we do not believe that the public interest would be served by adopting additional transfer restrictions under present circumstances.

13. At the same time, we are anxious to ensure that our recently adopted measures will prevent unjust enrichment. Therefore, we will adopt a measure expressly recommended in the subject statutory provision: transfer disclosure requirements. We note that there was no opposition to the adoption of this measure in the record. Specifically, we will require lottery applicants for voluntary transfer of control or assignment file with the Commission, along with their application, the consideration they will receive if the Commission grants their applications for voluntary transfer of control or assignment. These limited reporting

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[12] See, e.g., 47 C.F.R. §§ 22.920(c)(1)-(3), 22.927, 22.928, and 22.929 (cellular radio), and 95.819 and 95.821 (IVDS).

[13] See 47 C.F.R. § 94.47.

[14] Id. For this reason, we believe existing construction benchmarks and associated transfer restrictions adequately deter unjust enrichment in other services, such as the Specialized Mobile Radio Service (SMRs) and 220-222 MHz Private Land Mobile Radio Service.

requirements will enable the Commission to evaluate whether further restrictions are needed.[15] Such disclosures will also assist the Commission in drafting its mandatory report to Congress that will compare the results of the five-year auction experiment against the Commission's lottery experience. See 47 U.S.C. § 309(j)(12). In addition, transfer price disclosure rules will allow the secondary market to function efficiently under existing restrictions against unjust enrichment.

14. Accordingly, any applicant for voluntary transfer of control or assignment would be required to file, together with its application, the associated contracts for sale, option agreements, management agreements, or other documents disclosing the total consideration received in return for the transfer of its license. This information should include not only a monetary purchase price, but also any future, contingent, in-kind or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below-market financing). The Commission has existing procedures for maintaining the confidentiality of such filings.[16] The rules shall apply to any future applicant for voluntary transfer of control or assignment where the subject license was acquired by the transferor or assignor through a Commission lottery.

CONCLUSION

15. Because any rules adopted pursuant to Section 309(i)(4)(C) of the Communications Act will apply to only a limited number of noncommercial services where speculation rarely occurs, and because the Commission has recently taken action in a variety of commercial services to achieve the same goal of the subject statutory provision, we limit our action at this time to the adoption of transfer disclosure rules. If the data we collect as a result of this requirement indicates that our existing rules are inadequate, we may adopt additional measures to deter unjust enrichment in the lottery context.

Final Regulatory Flexibility Analysis

18. A Final Regulatory Flexibility Analysis is contained in Appendix B to this order.

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[15] We note that in the case of Low Power Television, the only broadcasting service subject to lotteries, the Commission currently has transfer disclosure rules. See 47 C.F.R. §§ 73.3540, 73.3597 and FCC Form 345.

[16] 47 C.F.R. § 0.459.

Ordering Clause

19. Accordingly, IT IS ORDERED that Parts 1, 21, 22, 90, 94 and 95 of the Commission's Rules, 47 C.F.R. Parts 1, 21, 22, 90, 94 and 95 ARE AMENDED as set forth in the Appendix A. IT IS FURTHER ORDERED that these rules are effective 90 days after publication in the Federal Register.

20. Issuance of this First Report and Order is authorized under the Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, Title VI, section 6002, and Sections 154(i), 309(i), 303(j), and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 309(i), 303(j), and 303(r).

Contact Persons

21. For further information concerning this proceeding, contact Marc Martin or Kent Nakamura, Office of Plans and Policy, (202) 653-5940.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

Appendix A

FINAL RULE

Part 1 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

1. The authority citation for Part 1 continues to read as follows:

AUTHORITY: Secs. 4, 303, 48 Stat. 1066, 1082, as amended; 47 U.S.C.154, 303:Implement 5 U.S.C. 552 and 21 U.S.C. 853(a), unless otherwise noted.

2. Section 1.924 is amended by adding a new paragraph (d) to read as follows:

§ 1.924 Assignment or transfer of control, voluntary or involuntary.

(a) * * *

(d) An applicant for voluntary transfer of control or assignment under this section where the subject license was acquired by the transferor or assignor through a system of random selection shall, together with its application for transfer of control or assignment, file with the Commission the associated contracts for sale, option agreements, management agreements, or other documents disclosing the consideration that the applicant would receive in return for the transfer or assignment of its license. This information should include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below--market financing).

Part 21 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

3. The authority citation for Part 21 continues to read as follows:

AUTHORITY: Secs. 1, 2, 4, 201-205, 208, 215, 218, 303, 307, 313, 314, 403, 404, 410, 610; 48 Stat. as amended, 1064, 1066, 1070-1073, 1076, 1077, 1080, 1082, 1083, 1087, 1094, 1098, 1102; 47 U.S.C. 151, 154, 201-205, 208, 215, 218, 303, 307, 313, 314, 403, 404, 602; 47 U.S.C. 552.

4. Section 21.38 is amended by adding a new paragraph (g) to read as follows:

§ 21.38 Assignment or transfer of station authorization.

(a) * * *

(g) An applicant for voluntary transfer of control or assignment under this section where the subject license was acquired by the transferor or assignor through a system of random selection shall, together with its application for transfer of control or assignment, file with the Commission the associated contracts for sale, option agreements, management agreements, or other documents disclosing the total consideration that the applicant would receive in return for the transfer or assignment of its license. This information should include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below--market financing).

Part 22 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

5. The authority citation for Part 22 continues to read as follows:

AUTHORITY: 47 U.S.C. 154, 303, unless otherwise noted.

6. Section 22.39 is amended adding a new paragraph (d) to read as follows:

§ 22.39 Transfer of control or assignment of station authorization.

(a) * * *

(d) An applicant for voluntary transfer of control or assignment under this section where the subject license was acquired by the transferor or assignor through a system of random selection shall, together with its application for transfer of control or assignment, file with the Commission the associated contracts for sale, option agreements, management agreements, or other documents disclosing the total consideration that the applicant would receive in return for the transfer or assignment of its license. This information should include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below--market financing).

Part 90 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

7. The authority citation for Part 90 continues to read as follows:

AUTHORITY: Sections 4, 303, and 332, 48, Stat. 1066, 1082, as amended; 47 U.S.C. 154, 303 and 332, unless otherwise noted.

8. Section 90.153 is amended by adding two new sentences at the end of the existing sentence to read as follows:

§ 90.153 Transfer of control or assignment of station authorization.

An applicant for voluntary transfer of control or assignment under this section where the subject license was acquired by the transferor or assignor through a system of random selection shall, together with its application for transfer of control or assignment, file with the Commission the associated contracts for sale, option agreements, management agreements, or other documents disclosing the total consideration that the applicant would receive in return for the transfer or assignment of its license. This information should

include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below--market financing).

Part 94 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

9. The authority citation for Part 90 continues to read as follows:

AUTHORITY: Sections 4, 303, 48 Stat. 1066, 1082, as amended; 47 U.S.C. 154, 303, unless otherwise noted.

10. Section 94.47 is amended by adding a new paragraph (c) to read as follows:

§ 94.47 Transfer and assignment of station authorization.

(a) * * *

(c) An applicant for voluntary transfer of control or assignment under this section where the subject license was acquired by the transferor or assignor through a system of random selection shall, together with its application for transfer of control or assignment, file with the Commission the associated contracts for sale, option agreements, management agreements, or other documents disclosing the total consideration that the applicant would receive in return for the transfer or assignment of its license. This information should include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below--market financing).

Part 95 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

11. The authority citation for Part 95 continues to read as follows:

AUTHORITY: Sections 4, 303, 48 Stat. 1066, 1082, as amended; 47 U.S.C. 154, 303, unless otherwise noted.

12. Section 95.821 is amended by adding two new sentences after the existing sentence to read as follows:

§ 95.821 Application for transfer of control.

An applicant for voluntary transfer of control or assignment under this section where the subject license was acquired by the transferor or assignor through a system of random selection shall, together with its application for transfer of control or assignment, file with the Commission the associated contracts for sale, option agreements, management agreements, or other documents disclosing the total consideration that the applicant would receive in return for the transfer or assignment of its license. This information should include not only a monetary purchase price, but also any future, contingent, in-kind, or other consideration (e.g., management or consulting contracts either with or without an option to purchase; below--market financing).

* * * * *

Appendix B

Final Regulatory Flexibility Analysis

As required by Section 603 of the Regulatory Flexibility Act, the Commission prepared an Initial Regulatory Flexibility Analysis (IRFA) of the expected impact of the proposals contained in the Notice of Proposed Rule Making, PP Docket No. 93-253 on small entities. By this Order, the Commission responds to a Congressional directive contained in the Budget Act to consider measures to deter unjust enrichment in the lottery context. The Commission received no comments in response to the IRFA concerning unjust enrichment in the lottery context. As noted in the text of the Order, we considered and rejected more burdensome requirements designed to deter unjust enrichment, such as additional transfer restrictions for licensees that acquire their license by lottery. Rather, we adopted the less onerous transfer disclosure requirement that is expressly recommended in the Budget Act. In the case of some spectrum-based services, such as Low Power Television, entities that file transfer of control applications with the Commission are currently required to submit information similar to what the Commission explicitly requires by this Order: copies of documents that reveal the transfer price for a license. Further, in other services, applicants for voluntary transfer of control or assignment are currently required to submit information in support of their request. Inasmuch as any contracts, purchase agreements, or similar legal documents detailing the consideration received by the transferor or assignor will presumably already have been prepared by the parties to the transaction for their own purposes, attaching a copy of such documents to the application(s) submitted to the Commission should not prove onerous. Accordingly, the Commission does not believe this limited disclosure requirement adds a significant economic burden on small entities.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

FCC 94-115

In the Matter of	)	
	)	
Implementation of Sections 3(n)	)	
and 332 of the Communications Act	)	
	)	GN Docket No. 93-252
Regulatory Treatment of Mobile Services	)	
	)	

ORDER

Adopted: May 18, 1994 Released: May 19, 1994

By the Commission:

1. On March 7, 1994, the Commission released a Second Report and Order in the above-captioned proceeding which, among other things, redesignated the Commission's Rules for Personal Communications Services (PCS) from Part 99 to Part 24. See Second Report and Order in GN Docket No. 93-252, Appendix A, page 10, 59 F.R. 18499 (April 19, 1994). The effective date of this redesignation is July 18, 1994. Id. On May 10, 1994, the Commission released a Third Report and Order in PP Docket No. 93-253, Implementation of Section 309(j) of the Communications Act-Competitive Bidding, FCC 94-98, amending existing PCS rules and adding new subparts F and G to Part 24 of our Rules. These rule changes will become effective thirty days after publication in the Federal Register, or around June 20, 1994.

2. In order to reduce confusion and to avoid having different portions of Part 24 taking effect at different times, we have decided to accelerate the effective date of our action redesignating Part 99 of our Rules as Part 24. This action will have no substantive effect; its only result will be to accelerate the date on which rules currently in Part 99 of our Rules are redesignated under a new Part 24.

3. Accordingly, IT IS ORDERED that our action in the Second Report and Order in GN Docket No. 93-252 to the extent that it redesignated Part 99 of our Rules as Part 24 WILL BECOME EFFECTIVE 30 days after publication of this Order in the Federal Register. This action is taken pursuant to Sections 4(i), 303(r), and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. Secs. 154(i), 303(r), and 309(j).

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

FCC 94-123

Before the

FEDERAL COMMUNICATIONS COMMISSION

Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Section 309(j)	)	PP Docket No. 93-253
of the Communications Act -	)	
Competitive Bidding	)	

Memorandum Opinion and Order

Adopted: May 27, 1994 **Released:** July 14, 1994

By the Commission: Chairman Hundt dissenting and issuing a statement; Commissioners Ness and Chong not participating.

I. INTRODUCTION

1. On August 10, 1993, the Omnibus Budget Reconciliation Act 1993 (the "Budget Act") added a new Section 309(j) to the Communications Act, as amended, 47 U.S.C. §§ 151-713 (the Communications Act). This amendment to the Communications Act gives the Commission express authority to employ competitive bidding procedures to choose from among two or more mutually exclusive applications for initial licenses. The *Second Report and Order* in this proceeding established general rules and procedures to govern the competitive bidding process.[1] We indicated in the *Second Report and Order* that unless specifically excluded, mutually exclusive applications in the Public Mobile Services filed after July 26, 1993, including cellular service, would be subject to competitive bidding.[2] We also indicated that we would address in a separate action the applicability of competitive bidding or lottery procedures to certain cellular

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1 Implementation of Section 309(j) of the Communications Act - Competitive Bidding, PP Docket No. 93-253, Second Report and Order, FCC No. 94-61, released Apr. 20, 1994 (*Second Report and Order*). We began the rule making proceeding approximately six weeks after passage of the Budget Act. *See* Implementation of Section 309(j) of the Communications Act - Competitive Bidding, PP Docket No. 93-253, Notice of Proposed Rule Making, 8 FCC Rcd 7635 (1993) (*Notice*).

2 *See* Second Report and Order at para. 61.

radio applications filed before July 26, 1993.[3]

2. In this Order, we state our intention to use lotteries to award licenses for all cellular unserved areas in which applications were filed prior to July 26, 1993. We conclude for the reasons set forth below that use of random selection instead of competitive bidding to award licenses among these competing applicants would serve the public interest.

II. BACKGROUND

A. *Lotteries for Cellular Unserved Areas*

3. In February 1990, the Commission initiated a proceeding to adopt rules to govern the acceptance, processing, and selection of applications for authority to operate initial cellular systems[4] in unserved areas of cellular markets.[5] Subsequently, in 1991 the Commission adopted lottery procedures for selecting applications for unserved areas.[6] In so doing, however, we stated that we would revisit our decision to use lotteries for unserved area applications if we received Congressional authority to conduct competitive bidding.[7]

4. As of April 11, 1994, we have received 10,900 unserved area applications for approximately 146 markets/blocks. Of these applications, all but two were filed prior to July 26, 1993. The Commission had scheduled two lotteries for these applications, but subsequently postponed the lotteries pending evaluation of the provisions of the Budget Act and possible implementation of competitive bidding procedures.[8]

B. *Budget Act Authority to License by Auctions and Lotteries*

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3 *See id.* at para. 60, n. 55.

4 Cellular Service is governed by Part 22 of the Commission's Rules. *See* 47 C.F.R. Part 22.

5 The unserved areas are generally within the borders of cellular markets, namely Metropolitan Statistical Areas (MSAs), Rural Service Areas (RSAs), and the Gulf of Mexico Statistical Area (GMSAs). Two cellular systems are licensed in each market on separate frequency blocks. Each initial cellular licensee in the MSAs and RSAs was given five years from the date of initial authorization to build and expand its system within its market. The geographic area not covered by each licensee on each frequency block is considered "unserved area." *See* Notice of Proposed Rule Making in CC Docket No. 90-6, 5 FCC Rcd 1044 (1990).

6 First Report and Order and Memorandum Opinion and Order on Reconsideration in CC Docket 90-6, 6 FCC Rcd 6185 (1991) (*First Report and Order).*

7 *Id.* at 6217.

8 *See* Lottery Notice, Mimeo No. 34917 (Sept. 16, 1993).

5. Section 309(j)(1) of the Communications Act permits use of competitive bidding procedures only for mutually exclusive applications for initial licenses or construction permits. Section 309(j)(2) provides that competitive bidding may apply to a particular use of the electromagnetic spectrum if the Commission determines that the principal use of the spectrum will involve, or is reasonably likely to involve, the receipt of compensation by the licensee from subscribers in return for enabling those subscribers to receive or transmit communications signals.

6. The Budget Act also amended Section 309(i) of the Communications Act[9] which provides for random selection of licensees. As amended, this section grants the Commission the authority to use random selection if there is more than one application for an initial license or construction permit that will involve the use of spectrum for a service that is not among the subscription-based services described in Section 309(j)(2)(A).[10] The Budget Act also includes a "Special Rule" limiting the use of random selection.[11] The Special Rule provides that the Commission shall not use random selection to award any license or permit after August 10, 1993, unless the Commission has determined that the use of spectrum is not for the provision of a subscription-based service within the scope of Section 309(j)(2)(A) of the Act, or that one or more applications for such licenses were accepted for filing by the Commission before July 26, 1993.[12]

C. Notice and Position of the Parties

7. In the *Notice*, we concluded that in light of the criteria set forth in Section 309(j) and the Special Rule, the Commission has the discretion to select licensees for the unserved area applications filed prior to July 26, 1993 by auction rather than by lottery. Therefore, we proposed to subject these pending applications to competitive bidding procedures, and we sought comment on this proposal.[13]

8. The commenters overwhelmingly oppose the proposal to apply the competitive bidding process to the cellular unserved area applications filed prior to July 26, 1993. They argue that for the Commission to move from lotteries to auctions for these pending applications would delay service to the unserved areas;[14] would be unfair to those applicants who relied in

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9 47 U.S.C. § 309(i).

10 *See* 47 U.S.C. § 309(i)(1)(B).

11 Budget Act, § 6002(e).

12 *Id.*

13 *Notice*, 8 FCC Rcd at 7662.

14 *See, e.g.*, Small RSA Operators Comments at 8, 12.

good faith upon the existing lottery procedures;[15] would cause financial harm and economic dislocation to thousands of applicants, many of whom are small business owners;[16] and would constitute an impermissible retroactive application of administrative rules and law.[17]

9. In the *Notice*, we also asked whether the Commission should allow full market settlements in these markets pending the decision to proceed by lottery or auctions. The commenters favor adhering to the existing cellular settlement policies. For example, Thumb Cellular Limited Partnership comments that for reasons of effectuating legislative intent and public policy, the Commission should permit settlements in order to avoid mutual exclusivity in cellular unserved areas and proceed with licensing rather than awaiting lotteries or auction proceedings.[18] The Cellular Settlement Groups point out that the Commission has a well-established policy favoring full-market settlements of contested applications.[19] Furthermore, they argue that the Budget Act indicates that Congress intended the Commission to proceed with its existing cellular settlement policies.[20]

III. DISCUSSION

10. Based on the record before us, we believe that the Congressional intent and the public interest would best be served by using the statutory lottery procedures for the unserved area applications filed prior to July 26, 1993. We agree with the commenters that use of the existing lottery procedures for the markets for which applications have been pending would be consistent with the congressional intent and would serve the public interest.

11. In the *Notice,* we determined that there are compelling public interest justifications for using lotteries rather than auctions for most services for which applications had been filed before July 26, 1993. *Notice* at para. 149. Thus, we proposed to lottery MDS applications filed before July 26th in order to avoid delays in service to the public that might result from awaiting the implementation of auction rules and noted that these applicants had already incurred substantial delays. In September, 1993, we also used lotteries to issue licenses to IVDS

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15 *See, e.g.,* Van R. Boyette Comments at 1; John Dudinsky Comments at 1.

16 *See, e.g.,* The Quick Call Group Comments at 1; David F. Gencarelli Comments at 1; Thomas Crema Comments at 1.

17 *See, e.g.,* The Coalition for Equity in Licensing Comments at 5-11; Wendy C. Coleman d/b/a WCC Cellular Comments at 5-11.

18 Thumb Cellular Limited Partnership Comments at 1-5.

19 Cellular Settlement Groups Comments at 6.

20 *Id.* at 7.

applications that were filed before July 26, 1993. *Notice* at para. 143, n. 150. We proposed in the *Notice* to use auctions for unserved area cellular applications and have examined the merits of this issue thoroughly. *Notice* at para. 160.

12. We have now decided not to use auctions for these services. As explained below, any concern that some speculative applications might have been filed for these cellular markets does not, by itself, justify the use of auctions in these circumstances. Rather, equitable factors must also be considered and balanced against that concern. We also believe that any concern regarding speculative applicants is mitigated considerably in view of the current rules governing cellular unserved areas. Our rules require that all facilities proposed in the application be constructed and service to the public be initiated within one year from the grant of the authorization. In addition, licensees may not transfer unserved area authorizations until after the facilities have been providing service for one year. As we indicated in the *First Report and Order,* these rules were adopted to provide service to the public as expeditiously as possible and to deter speculation.[21] Moreover, random selection of cellular unserved area licenses may increase the likelihood of new entrants offering service in the cellular marketplace.

13. The legislative history also demonstrates that Congress recognized the equities involved in the auction law's grandfathering provisions for applications on file with the Commission before July 26, 1993. For example, Congress in the Conference Report explicitly singled out the pre-July 26th applicants in the IVDS service as examples of applicants for whom the Commission would be permitted to use lotteries. H.R. Rep. No. 213, 103d Cong., 1st Sess. 498 (1993) ("Conference Report"). From this, we infer that, whatever concerns Congress had about the possibility of speculative applications in particular services, Congress ultimately decided that other factors, including considerations of equity and administrative cost and efficiency, justified the use of lotteries for those applicants who, in reliance on the Commission's existing lottery procedures, had filed applications prior to July 26th.

14. Consistent with the considerations that motivated Congress to enact the grandfathering provision, the commenters point out that many of these cellular unserved area applications have been on file for more than a year.[22] Further, they point out that these applicants' business plans did not take into account the additional expenditures that they would incur if licenses were to be awarded by competitive bidding. These arguments are, we believe, valid ones. Indeed, as a practical matter, we believe that existing applications for cellular unserved areas provide no indication that the applicants have any interest at all in participating in auctions. To ensure successful auctions, therefore, we would have to allow these applicants to clarify their intentions and to submit the information required by Section 1.2105 of our Rules. In fairness to existing applicants, moreover, those who indicate no desire to participate

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21 *First Report and Order* at 6223-25.

22 *See, e.g.,* Cole, Raywid & Braverman Comments at 1; The Coalition for Equity in Licensing Comments at 18.

in auctions should also be entitled to a refund of their application processing fees. In sum, if we were to use auctions, the whole application process must begin anew at a considerable cost to the 10,900 applicants and to the Commission.

15. Another factor that militates against the use of auctions is the questionable commercial value of the cellular unserved areas. Cellular unserved areas vary in geographic size and population coverage. Few markets would be likely to attract significant bids. As for the others, it is unclear whether the bids that would be submitted for most markets would be substantial enough to create an economic incentive to construct the facilities more efficiently.[23] It would be difficult to articulate a principled basis for distinguishing between markets that would be auctioned and markets that would be subject to lotteries. Finally, we believe that using auctions for the cellular unserved area applications would be inconsistent with the Commission's decision to use lotteries for IVDS applications that were filed prior to July 26, 1993.

16. On further reflection, therefore, we are not persuaded that either Congress's intentions or the public interest support the administrative upheaval and dislocation in business plans that would result from the use of auctions in these circumstances. Indeed, no assurance even exists that using auctions for these particular applications would expedite the deployment of service to the public, a principal objective of the auction law. It has been estimated that it may take 60 days or longer to complete an auction than to complete a lottery. We believe that such estimates must take into account other possible factors creating administrative confusion and attendant delays, such as the time that may be needed to accept new applications from new parties, the time to allow current applications to be returned and refunds issued, and the time for current applicants to refile their applications under the auction process. The delay inherent in completing the administrative process of calling for and reprocessing these applications might even exceed the time savings that might result from discouraging possible speculative applications. In addition, in view of the currently scheduled auctions for narrowband PCS and IVDS applications in late July, it is unlikely that auctions could be held for cellular unserved areas in the immediate future.

17. In contrast, if we employ lotteries, we will be able to proceed almost immediately to issue authorizations for these services. As we indicated in our First Report and Order in this proceeding, we believe our existing build-out rules are likely to have a substantial impact in ensuring that service is implemented promptly.[24] We are also convinced that using the lottery

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23 While Chairman Hundt in his dissent proposes a bifurcated process that uses auctions for "properties of meaningful value" and lotteries for the remaining markets, we believe that using the lottery process is the most consistent and the fairest method for dealing with all unserved area applications filed before July 26, 1993. Indeed, it is not clear that the Budget authorizes such a bifurcated procedure.

24 *See* First Report and Order in PP Docket No. 93-253, FCC 94-32, released February 4, 1994 (*First Report and Order*) at para. 9.

process for the cellular unserved area applications filed before July 26, 1993 provides an opportunity to make these systems available to new competitors in a very short period of time. Further, these new cellular unserved licensees could eventually seek joint ventures with PCS providers to offer expanded services in these markets. Therefore, taking all of these factors into account, we agree with commenters that auctions should not be used for these applications. Rather, we conclude the public interest would be furthered by using lotteries. The use of lotteries for applications filed before July 26, 1993 comports with Congressional intent.

18. For the same reasons that we are proceeding with the lotteries, we believe that it is in the public interest to utilize the full market settlement policies that apply to the cellular unserved area applications. Allowing those parties who have entered into full market settlements to proceed with licensing will expedite service to the public without expending further Commission and private resources.

IV. CONCLUSION

19. In this *Order,* we state our intention to use existing random selection procedures to choose from among mutually exclusive applications filed prior to July 26, 1993, for authorization to provide cellular service to unserved areas. This conclusion is consistent with the Special Rule adopted in Section 6002(e) of the Budget Act. In the near future, we will issue a Public Notice rescheduling the two previously scheduled lotteries. Finally, we will consider requests for approval of full market settlements and proceed with licensing where such approval is granted. We are confident that these decisions will expedite service to the public.

V. ORDERING CLAUSES

20. Accordingly, IT IS ORDERED that selection from among mutually exclusive applications filed prior to July 26, 1993, to provide cellular service to unserved areas shall be by random selection, in accordance with existing Commission rules, as set forth above.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

Dissenting Statement
of
Chairman Reed E. Hundt

Implementation of Section 309(j) of the Communications Act - Competitive Bidding for Cellular Unserved Areas (PP Docket No. 93-253)

The Commission's September 1993 Notice in the Competitive Bidding proceeding proposed that we use competitive bidding to award unserved area cellular licenses. [1] I concur in the Notice's tentative conclusion that competitive bidding is a better approach for awarding these licenses than lotteries. I accordingly dissent from my fellow Commissioners' decision to use lotteries for the unserved cellular area applications at issue in this proceeding. I greatly respect my colleagues' decisionmaking, but I am deeply troubled, for the reasons set forth below, by the prospect of giving away tens of millions of dollars (or more!) in public property -- spectrum -- by means of a lottery. That technique, in my judgment, does not serve any significant public policy goals, and certainly inflicts much harm on the public interest.

Unserved cellular areas are those geographic portions of an initial cellular licensee's market that the licensee fails to serve within five years of its service authorization, at which point these areas become available for separate licensing. Under the Omnibus Budget Reconciliation Act of 1993 (the "Budget Act"), the Commission has the discretion to award

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[1] See Implementation of Section 309(j) of the Communications Act -- Competitive Bidding, Notice of Proposed Rule Making, PP Docket No. 93-253, Para. 160 (released October 12, 1993) (Auction Notice).

licenses for those cellular unserved area applications filed before July 26, 1993, by either lottery or auction. It is important to note, however, that the Budget Act clearly suggests that the Commission should use auctions for applications filed before that date when auctions would further the public interest objectives of the Act more effectively than awarding the licenses by lottery.

Instead of evaluating this issue based on the public interest objectives of the Budget Act, the majority bases its conclusion that lotteries should be used to award licenses for applications filed before July 26, 1993, on the grounds that considerations of equity, administrative cost and efficiency justify lotteries for those applicants that relied on the Commission's lottery procedures in filing their applications.

In my view, none of these considerations is persuasive. First, in support of their concern with equity, the majority notes that many of these applications have been on file for more than a year, and that applicants' business plans did not take into account the additional expenditures entailed in auctions. The majority also relies on the suggestion of some commenters that switching from lotteries to auctions would cause financial harm and economic dislocation to many applicants.

This concern, however, is offset by the fundamental realities of the lottery process, as repeatedly experienced by this Commission. The Commission's extensive experience with cellular lotteries overwhelmingly demonstrates that lotteries inevitably attract applicants that

have no interest in building and operating cellular systems in the long term or in providing quality service to customers in the unserved areas. Moreover, even those who might take exception to this proposition must agree that only an auction can award a license to the applicant that most highly values a license. These are some of the reasons that the Commission so forcefully supported the Congressional grant of auction authority. Nor should anyone ignore the grave deficiencies of the lottery practice -- even without attending to the fact that the public fisc gains nothing from the lottery. This Commission's experience with lotteries in awarding cellular licenses demonstrates that lottery winners rarely intend to build and operate the cellular system proposed in their applications -- in fact, approximately 85% of non-wireline cellular licenses changed hands after the initial lotteries. The evidence suggests that lottery applicants are unlikely to invest time or money in developing detailed business plans to provide cellular service; indeed, given the arbitrary nature of lotteries, an applicant has little incentive to develop such a plan until it actually wins a lottery. Any applicants that are bona fide businesses seeking to provide cellular service in an unserved area would undoubtedly prefer the predictability of an auction to the randomness of a lottery.

Second, the majority suggests that an auction would entail considerable additional administrative costs. There is no evidence in the record to suggest the auctions would create significant additional administrative costs as compared to lotteries for this Commission. We have already developed auction procedures for other services covered by the Budget Act, and adapting these procedures and conducting auctions for cellular unserved area applications

filed before July 26, 1993, would not entail significant additional expense.

Third, the majority further suggests that an auction approach would be less efficient than a lottery. As we have already done for other services, we should address this concern by choosing an auction procedure for unserved areas that is simple and efficient. (An example would be a single round of sealed written bids.) In any event, we should consider not only the efficiency of the award process, but also the effectiveness of that process in ensuring that customers receive service from the new licensee as soon as possible. Auction winners are guaranteed to be better prepared and to have a greater incentive than lottery winners to provide better service faster to unserved areas -- generally because they have paid money for their licenses.

In short, the record does not support a conclusion that auctions would entail more "administrative upheaval and dislocation in business plans" than would occur with lotteries. Nor does the record provide any significant evidence that equitable, cost or efficiency considerations dictate that lotteries should be used to award these licenses.

In fact, the public interest factors of the Budget Act all dictate that auctions would better serve the public interest under the Act than lotteries.

The first public interest objective of the Budget Act is the promotion of "the development and rapid deployment of new technologies, products, and services for the

benefit of the public, including those residing in rural areas, without administrative or judicial delays." The majority suggests that no assurance exists that auctions would expedite service in furtherance of this objective, and observes that any speed that might be achieved by discouraging speculative applications could be eroded by the additional time required to conduct auctions. I believe the evidence supports the Notice's tentative conclusion that auctions do in fact expedite service to the public in unserved cellular areas because insincere applicants that do not intend to build out their systems would be discouraged from competing in an auction.[2] As noted above, the vast majority of the winners in our prior cellular lotteries sold their licenses after the lottery. That is very likely to happen here, unless by freakish chance the lottery winner proves to be a firm that would have submitted the winning bid in an auction. The result of the lottery, therefore, will be to transfer the tens of millions of dollars to be paid by these firms in auctions from the government to the lottery winner. It is not a personal judgment on these winners to say that they do not deserve the public's money.

As a result of our experience with cellular lotteries, we tightened our rules to eliminate many of the shortcomings that provided immediate, post-award windfalls to lottery winners and caused unacceptable delays in delivering service to the public in the lotteried markets. Even so, I do not believe that these revisions change the fact that cellular lotteries do not necessarily attract applicants that are fully committed to providing cellular service to customers in the unserved areas. Many, if not most, lottery applicants are not prepared for

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[2] See Auction Notice at Para. 160.

or experienced in building and operating cellular facilities. If prior experience is any guide, lottery winners for the unserved cellular areas will devote their efforts during the post-award period to finding other entities that will provide the necessary financing and technical expertise needed to help them construct their systems in time to avoid forfeiting their licenses. This process usually consumes weeks and months, resulting in additional and, in my view, unnecessary delay before consumers in these unserved areas finally have access to modern cellular telephone service from these licensees. By contrast, licensees that acquire their service area in an auction have a compelling incentive to begin earning a return on their investment in the license as soon as possible by expeditiously constructing their facilities and providing service to the public.

It is at least arguable that lotteries could be conducted sooner than auctions -- but not by any meaningful time period. However, if we moved promptly, it could take fewer than 60 additional days to conduct auctions for the unserved areas, as compared to a lottery process. This hypothetical (but in all events short) time difference in the pre-award period could be more than offset by the auction winners' incentive to build out their service areas quickly, as compared to the extra time it would take an unprepared lottery winner to accomplish the same task. In short, from the public's perspective, auctions will result in more rapid deployment of service in unserved areas than lotteries. After many years of waiting in some unserved areas, customers deserve service sooner rather than later, and auctions would give us that result.

The Budget Act's second public interest objective is to promote economic opportunity and competition and ensure that new and innovative technologies are readily accessible to the public by encouraging small businesses, rural telephone companies, and businesses owned by minorities and women to become licensees. Auctions that include meaningful preferences for these designated entities would afford such applicants that genuinely wished to provide cellular service to the public a more realistic opportunity to obtain a cellular license than if they were subject to the whims of a lottery. Lottery applicants that did not ultimately wish to provide service would likely drop out of an auction and seek a refund of their filing fee, giving new designated entity entrants that really want to enter this market a better shot at obtaining a license than if they were merely participating in a random lottery. To elect a lottery method means to disregard the goal of including small businesses, women, and minorities as fair participants in the opportunity of providing cellular services in the subject areas.

The third public interest objective of the Budget Act is recovery of a portion of the value of the public spectrum resource for the benefit of the public. Although the record does not indicate the precise amounts that potential businesses could bid for these cellular unserved areas, we do know that hundreds of applications have been filed for some of these markets. For example, 513 applications were filed for the Los Angeles frequency block B unserved area, and 11 other markets drew more than 400 applications each. I believe conducting auctions for cellular unserved markets has the potential of generating substantial sums for the U.S. Treasury, as Congress intended in the Budget Act. The evidence suggests

that it is reasonable to expect that these unserved cellular auctions would generate revenues of as much as $32 million, and perhaps significantly more.[3] Certainly the Commission has no evidence to disprove these estimates. In fact, there is no evidence in the record to support any contention that the auction of these licenses would draw only insignificant bids. I see no reason to deprive the U.S. Treasury of meaningful tangible revenues, particularly if we simply propose to give these spectrum licenses away in a lottery to applicants that are likely to resell them privately for significant amounts as soon as our rules permit such a transfer. In addition to being inconsistent with the intent of Congress, using a lottery for these cellular unserved areas would produce the incongruous result of needlessly giving away valuable spectrum at the same time we are conducting auctions for other potentially less valuable properties.

I recognize that each and every cellular unserved property would not necessarily generate significant revenues in an auction. Indeed, it might not be appropriate to auction unserved cellular markets that are of such low value that the revenues generated would not justify the effort and expense of an auction for the participants. We could, however, sort out such properties by setting a reservation price (say, $50,000) for the cellular unserved auctions which bidders would have to meet or exceed in order to receive the license. If no bids were received at or above a specified level, the Commission could promptly conduct a lottery to award the license to one of the pending applicants. This dual approach, perfectly

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[3] See Letter from G. Salemme, McCaw Cellular Communications, Inc. to W. Caton, Acting Secretary, Federal Communications Commission (May 13, 1994)

consistent with the statute, would ensure the public would receive the financial and quality of service benefits from auctioning licenses in markets that have commercial value, while allowing use of lotteries in markets where auctions do not produce the desired incentive to proceed promptly with construction.

The Budget Act directs us to use the technique of competitive bidding where it is more likely than the lottery method to lead to efficient use of the electromagnetic spectrum. An auction winner for an unserved cellular area will have an economic incentive to design and build its system to offer low-cost service to the public by, among other things, using spectrum-efficient technology that minimizes the need for future upgrades of its facilities to accommodate spectrum shortages. By contrast, a lottery winner that anticipated the subsequent sale of its license as soon as our rules permit would be more likely to build out its system as quickly as possible using relatively inexpensive, spectrum-inefficient technology in order to meet its deadline under our rules.

I think it also bears emphasis that my conclusion that auctions should be used, wherever economically feasible, to award licenses for unserved cellular areas is the same conclusion that this Commission tentatively reached in the Notice of Proposed Rule Making. In that Notice, the Commission unanimously proposed the use of auctions for these licenses on the grounds that it would discourage insincere applicants and "provide more opportunity for a wider variety of applicants to become cellular licensees."[4] For the reasons set forth

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[4] Auction Notice at Para. 160.

above in this Dissenting Statement, I see no basis in the extensive record in this proceeding for changing this well-reasoned conclusion.

In sum, the Congressional intent reflected in the public interest objectives of the Budget Act requires us in my view to subject mutually exclusive applications for cellular unserved areas to auctions whether they were filed before or after July 26, 1993. Competitive bidding is a better way than lotteries to serve the interests of consumers and service providers alike.

Before the
Federal Communications Commission
Washington, D.C. 20554

FCC 94-199

In the Matter Of	)	
	)	
Amendment of Part 36 of The Commission's Rules And Establishment of a Joint Board	)	CC Docket No. 80-286

NOTICE OF INQUIRY

Adopted: August 2, 1994; Released: August 30, 1994.

By the Commission:

Comment Date: Friday, October 28, 1994.

Reply Comment Date: Friday, December 2, 1994.

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I. INTRODUCTION

1. In this Notice of Inquiry (Notice), we seek to develop information concerning the manner in which our Part 36 jurisdictional separations rules are used to provide interstate assistance to local exchange carriers ("LECs"). Currently, LEC study areas[1] with greater than average costs per loop[2] receive high-cost assistance from the Universal Service Fund ("USF").[3] In addition, study areas with fewer than 50,000 loops receive interstate assistance for their local switching costs through the application of a multiplier to their interstate usage of local switching equipment.[4]

2. The Notice invites comment on various policy questions relating to the provision of high-cost assistance.[5] It also seeks comment on the goals of high-cost assistance, and on whether high-cost assistance should be used to promote facilities modernization, in addition to supporting nationwide availability of telephone service at affordable rates. We ask commenters to address the appropriate level and targeting of high-cost assistance and to evaluate the relationship between high-cost assistance and the development of competition in local services. We also request comment upon a number of alternatives for changing the present high-cost assistance mechanisms. These alternatives would take two primary approaches: the first is based upon individual reported costs, as are the present USF rules; and the second is based upon

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[1]A study area is the area within a single state jurisdiction where a LEC provides local telephone service. No changes have been permitted in study area boundaries since November 15, 1984, except with special permission of the Commission. See 47 C.F.R. Part 36, Appendix-Glossary (1993).

[2]A loop is "[a] pair of wires, or its equivalent, between a [local telephone] customer's station and the central office from which the station is served." 47 C.F.R. Part 36, Appendix-Glossary (1993).

[3]The basis for a LEC study area's receipt of high-cost assistance is its "average unseparated loop cost per working loop," 47 C.F.R. §36.631 (1993), a term which is defined in 47 C.F.R. §36.622 (1993). Hereinafter in this Notice we shall refer to such cost as "cost per loop."

[4]This means of assistance, known as dial equipment minute ("DEM") weighting, is discussed at greater length in the "Appendix" to this Notice. See 47 C.F.R. §36.125 (1993).

[5] We previously referred the issue of general changes in the Part 36 rules governing the USF to the Federal State Joint Board in this proceeding, but stated that a further notice of proposed rulemaking addressing possible permanent changes in the Part 36 USF rules would be necessary. Amendment of Part 36 of the Commissions Rules and the Establishment of a Joint Board, 8 FCC Rcd 7114 (1993) (Interim Notice). This Notice of Inquiry is designed to focus the issues in advance of that further notice of proposed rulemaking.

factors designed to reflect general cost characteristics and economic conditions. Finally, we invite comment upon the need for a transition mechanism in the event we modify or replace the existing high-cost assistance rules.

II. BACKGROUND OF HIGH-COST ASSISTANCE

3. It has been more than nine years since we originally decided to implement high-cost assistance by adopting our USF rules. Nearly seven years have elapsed since we adopted the DEM weighting assistance program for small study areas in order to ameliorate potential jurisdictional cost shifts associated with changes in the classification of local switching equipment. Last year, the gradual phase-in of the USF and DEM weighting was completed. We believe that it is appropriate at this time to consider how well the USF and DEM weighting subsidy programs have achieved their objectives and to evaluate whether changes, large or small, would make these programs more effective. Reevaluation of our high-cost assistance rules should not, however, be limited to fine-tuning or review of past performance. The need to consider changes to high-cost assistance mechanisms is broad-based and fundamental.

4. The USF was first adopted by this Commission in 1984 in conjunction with the establishment of fixed percentage basic allocation factors for jurisdictional separation of non-traffic-sensitive ("NTS") costs.[6] The USF was intended to promote universally available telephone service at affordable rates.[7] Before the USF rules were implemented, we modified the USF structure, adopting a two-tiered system of assistance which increased support for small LECs and decreased assistance to larger LECs.[8] Three years later, we readjusted the USF by further increasing assistance to small LECs and decreasing assistance to large LECs.[9] The USF and the basic allocation factors were phased

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[6]Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 96 F.C.C. 2d 781 (1984) (Initial USF Order). See "Appendix" at 23-25, paras. 1-7, for a more extensive discussion of the history of the USF.

[7]96 F.C.C.2d at 794, para. 29.

[8]MTS and WATS Market Structure; and Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 50 Fed.Reg. 939 (January 8, 1985) (1984 Retargeting Order), adopting the recommendation of the Federal-State Joint Board, 49 Fed.Reg. 48325, 48335-36 (December 12, 1984) (1984 Retargeting Recommendation).

[9]MTS and WATS Market Structure; and Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 2 FCC Rcd 2953 (1987) (1987 Retargeting Order).

in during a seven-year transition period, beginning in 1986 and concluding in 1993.

5. Since our initial adoption of the USF in 1984, changes in technological capabilities and costs, market structure, and regulatory options have revolutionized the telecommunications marketplace. At this point in time, the conversion to equal access is virtually complete, interexchange competition is increasingly robust, cellular services are widely available, fiber optic facilities have been deployed extensively for both nationwide backbone networks and local access purposes, and other technologies and services, such as cable television and personal communications service, may, in the near future, offer services that are functionally equivalent to today's switched telephone service. We also note the efforts of many private companies to extend the reach of their networks by taking steps to include the connection of classrooms, libraries, and healthcare facilities to the telecommunications infrastructure as part of their investment planning. In addition, new forms of regulation, including incentive-based approaches such as price caps, have been adopted in numerous jurisdictions.

6. We recognize that as technologies change, it may be necessary in the future for the Commission to undertake a comprehensive review of our universal service goals. At this time, in light of the numerous changes in the telecommunications industry since our initial adoption of the USF, we believe it is incumbent upon us to chart a course for high-cost assistance that acknowledges the state of today's telecommunications industry and makes provision for tomorrow's developments. We now have several years of experience with USF high-cost assistance. The availability of historical data should facilitate productive evaluation of the existing mechanisms. We expect to use this information to assess the effectiveness of the current USF rules, in light of the present and future goals of high-cost assistance. We also intend to consider issues related to the total amount of high-cost assistance, as well as the rate[10] and pattern of growth in the amount of assistance.[11] For these reasons, it is appropriate at this time to review and to evaluate the targeting and overall growth of the USF as currently structured, and to obtain comment on possible revisions.

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[10]See 1984 Retargeting Recommendation, 49 Fed.Reg. at 48336, ¶58 ("We recognize...that rapid growth in the amount of high-cost assistance could necessitate reexamination of the high cost formula").

[11]See Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, 8 FCC Rcd 7114 (1993) (Interim Notice), 9 FCC Rcd 334 (1993) (Interim Recommendation), and 9 FCC Rcd 303 (1993) (Interim Order).

7. Similarly, the time is ripe for us to examine the purposes and effects of DEM weighting assistance. When first adopted in 1987, DEM weighting was intended to ameliorate the potential adverse effect on some small LECs of eliminating the NTS allocation previously used in the jurisdictional separation of local switching equipment.[12] In recent years, however, DEM weighting has appeared to give an incentive to some LECs to manipulate our separations rules as they categorize their costs associated with certain types of equipment.[13] Now, at the conclusion of the transition period for phasing in DEM weighting, we seek information on a number of issues related to this form of assistance. Among those issues are questions relating to the total amount of assistance provided through DEM weighting, the necessity of continuing DEM weighting on a permanent basis, the targeting of DEM weighting, and the possibility of restructuring the DEM weighting assistance mechanism or combining it with the USF assistance program.

8. This Notice seeks information on two principal approaches to revising our high-cost assistance mechanisms. The first approach, which would continue to base high-cost support upon recipients' reported costs, would entail a number of possible modifications to the existing USF and DEM weighting rules. The second approach would replace the current cost-based USF assistance mechanisms with a system providing high-cost assistance based upon one or more factors that would serve as a proxy for reasonable costs. The use of proxy factors would create a direct incentive for recipients to reduce their cost of providing service, unlike the current USF mechanisms, that base the assistance provided to service providers upon their reported costs. We ask that interested parties consider both the individual alternatives presented in this Notice as well as the possibility of combining various alternatives to produce an optimal system of high-cost assistance.

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[12]DEM weighting provides interstate assistance to small LECs by allowing qualifying LEC study areas to allocate their separations Category 3 central office equipment local switching costs to the interstate jurisdiction on the basis of prescribed DEM weighting factors. Under our rules, small LECs multiply their actual interstate switching minutes by the weighting factors, thereby increasing their interstate allocations. See "Appendix" at 25-26, paras. 8-11.

[13]See Responsible Accounting Officer Letter No. 21, Classification of Remote Central Office Equipment for Accounting Purposes, 7 FCC Rcd 6075 (Acct. and Audits Div. 1992) (RAO 21), petitions for recon. pending.

III. General Issues Relating to High-Cost Assistance

9. In this Notice, we request comment on a number of measures for revising the high-cost assistance mechanisms contained in our rules. These alternatives span a broad spectrum, ranging from modification of the existing rules to implementation of an entirely new system of high-cost assistance. We request interested parties to comment upon the various alternatives in light of the broader issues discussed below.

10. High-cost assistance quite obviously must serve the goals underlying the principle of universal service. For example, high-cost assistance can play a role in preserving and enhancing universal telecommunications services and just and reasonable rates. In furtherance of the goal of universal service, however, the high-cost mechanisms ultimately adopted should reflect the most efficient use of resources to promote universal service, so that they do not inadvertently impose excessive burdens on either users or services that provide assistance. We believe that an efficient system of high-cost assistance should display three primary characteristics.

11. First, assistance should be tailored so that only those users or service providers who need assistance to ensure universal service receive support. We ask the commenters to focus carefully on the targeting structure and effect of the various alternatives for revision of our high-cost assistance mechanisms.

12. Second, an optimal high-cost assistance mechanism should promote efficient investment and operation. Incentives to engage in "goldplating," or to invest in certain types of facilities when other facilities would be more economically efficient, should be eliminated or minimized, if it is possible to do so without significant harm to other public policy goals. Similarly, the high-cost assistance mechanisms should not create artificial incentives for carriers to sell or acquire facilities.[14] We invite the commenters to discuss the extent to which the various alternatives display this quality.

13. Third, the best high-cost assistance mechanism would not impose excessive subsidy costs upon interstate carriers and ratepayers. An efficient and properly structured system of high-cost assistance should make it possible to minimize the cost of assistance while still providing adequate support to its recipients. Thus, the overall amount of assistance should reflect a balancing of universal service goals with our desire to avoid placing an unreasonable burden upon interstate telecommunication.

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[14]For example, revised high-cost assistance rules should eliminate or reduce the current incentives for large LECs to sell high cost exchanges to smaller LECs.

We remain confident that an efficiently targeted system of high-cost assistance can serve all of those goals.

14. Before describing specific alternatives for revising our USF and DEM weighting rules, we must examine the goals to be served by our high-cost assistance programs. The pertinent Joint Board recommendations as well as our orders are replete with references to the intention that the USF promote affordable local rates, lower than the rates would be absent high-cost support.[15] Implicit in the goal of high-cost assistance was the notion that "universal service would be threatened by rate increases of a magnitude sufficient to cause a significant number of subscribers to cancel service."[16] We believe that it is important to reconsider the purpose of high-cost assistance as part of our evaluation of the existing USF and DEM weighting rules and our consideration of possible replacement or refinement of those mechanisms.[17] We therefore request that interested parties comment upon whether high-cost assistance should be extended to support facilities modernization in addition to affordable local rate levels. We also ask whether high-cost assistance should be targeted to support basic services without providing assistance for more advanced service offerings.

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[15]Initial Notice ("the objective of mitigating the impact of high costs upon basic service rates," 47 Fed.Reg. at 54483, ¶108; "the goal of preventing unduly rapid local rate increases," Id. at ¶110); 1983 Recommendation (("The...high cost support mechanism we recommend today will help protect the nationwide availability of telephone service at reasonable rates," 48 Fed.Reg. at 46568, ¶63); Initial USF Order ("[The USF] will moderate local exchange rates in high cost areas," 96 F.C.C.2d at 792, ¶21; "We find that the basic provisions for the protection of universal service recommended by the Joint Board represent a sound balancing of concern for the promotion of universally available telephone service at reasonable rates and the need to prevent uneconomic bypass of the local exchange based on the information presently available," 96 Id. at 794, ¶29); 1984 Retargeting Recommendation ("We...wish to reemphasize our conclusion that the high cost assistance should be used exclusively to keep local telephone rates lower than they otherwise would be," 49 Fed.Reg. at 48336, ¶59); 1984 Retargeting Order ("the Joint Board has affirmed our view that high cost assistance, targeted to recognize the special situation of customers served by smaller, rural telephone companies, is necessary to preserve universal service," 50 Fed.Reg. at 942, ¶14).

[16]1984 Retargeting Order, 50 Fed.Reg. at 942, ¶12.

[17]We recognize that there are many broad issues concerning our overall universal service policy that are beyond the scope of this inquiry into the USF high-cost assistance program. We are also cognizant of our responsibility to address these issues in a timely manner. In that regard, we note that the National Telecommunications and Information Administration is initiating a broad inquiry to examine universal service issues. We intend to monitor the progress of that proceeding, because the information developed may be relevant to policy issues before us. Finally, information compiled in response to this Notice of Inquiry may be relevant to a broader examination of our universal service policy, such as those proposed in legislation now pending in Congress.

15. We also seek comment on the appropriate balance to strike between promoting the need for high-cost assistance and the need to avoid imposing unreasonable burdens directly upon interexchange carriers or other telecommunications service providers and indirectly upon their subscribers. We believe that it is crucial to target assistance in the most effective and efficient manner possible, in order to avoid imposing unnecessary costs that would cause large increases in the total subsidy level. We seek proposals for accomplishing such targeting. In a separate section of this Notice,[18] we request comment regarding customer vouchers that would target high-cost assistance to individual telecommunications users, similar to the current lifeline and link-up programs. Such an assistance structure could allow us to target assistance more precisely and to eliminate barriers to competitive entry that may be inherent in a system that provides assistance only to the established carriers.

16. High-cost assistance also could significantly affect the development and viability of competition in local telecommunications services. The existing USF and DEM weighting mechanisms, which give high-cost assistance only to LECs, may serve as barriers to entry by competing service providers. We ask parties to identify what measures, if any, might be taken to ensure that our high-cost assistance mechanisms do not act as de facto barriers to entry by giving existing LECs insurmountable cost advantages over potential competitors. Conversely, it is possible that the LECs' status as providers of last resort for basic telephone service gives potential competitors that do not share this obligation a cost advantage over LECs that serve both high cost and low cost areas.

17. Finally, we request parties to propose means by which we can ensure that high-cost assistance is used by recipients to offer their subscribers lower local telephone rates. High-cost assistance should not be used by recipients to increase their rates of return to excessive levels rather than to reduce their charges to local subscribers. We seek comment on ways to deter this and any other unintended and undesirable results. In addition, if we determine that high-cost assistance should be targeted to support specific services, we ask for comment on whether and how we could deter recipients from using high-cost assistance to subsidize other services. In particular, we request parties to comment upon the need to include attestation requirements or periodic audits as part of our high-cost assistance program. We also invite comment regarding the desirability of reporting requirements for assistance recipients' uses of fund revenues, local rate levels, and earned rates of return. Finally, we solicit proposals for implementing any or all of these requirements in a manner that would not be unduly burdensome to recipients.

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[18] See ¶¶ 78-80, infra.

IV. ALTERNATIVES FOR REVISING HIGH-COST ASSISTANCE

A. Determining and Controlling the Total Amount of High-Cost Assistance

18. In our recent Interim Notice, we expressed our concern over the relatively rapid growth of the USF during the past several years. Since its inception, the full-transition amount of the USF has grown nearly sixty percent, or almost seven percent per year. As we indicated, we believe that the time has arrived to determine whether USF growth of this magnitude is essential to promote universal service.

19. At present, the USF exceeds $700 million annually and DEM weighting, intended to benefit small LECs, adds another $300 million of annual assistance. We seek proposals for retargeting assistance to reduce the overall level of support while ensuring adequate support for those LECs or LEC customers genuinely in need of assistance. In addition, we request that commenters addressing the specific alternatives described below include in their comments an estimate of the total amount of high-cost assistance necessary to maintain universal service. Finally, we ask the commenters to compare the efficiency of the various alternatives for high-cost assistance, and to identify the measure or measures that would promote universal service while imposing the least costs upon interstate carriers and ratepayers.

20. After reviewing the record compiled in response to this Notice, we intend to propose specific revisions to our high-cost assistance mechanism that will allow us to reduce subsidy costs borne by interstate ratepayers while ensuring that universal service is not jeopardized in areas that require support. Because the USF is funded through interstate tariff charges paid by IXCs, increases in the USF may require IXCs to raise the interstate toll rates paid by telecommunications users. Such increases would depress demand for these interstate services. The implications for the telecommunications industry, and consequently for the general economy, are significant. For these reasons, the structure and magnitude of high-cost assistance are matters of considerable concern to this Commission.

21. In our recent Interim Order, we adopted interim rules employing an index factor to moderate growth in the USF pending adoption of final rules. As we noted in the Interim Order, growth in the USF has been erratic during the years that the fund has been in existence. That pattern of growth triggers questions regarding its cause, including the question of whether past growth reflected actual need for increased USF support or, instead, was a result of unanticipated defects in the structure of our assistance mechanisms. In the future, we wish to avoid, to the extent possible, unjustified surges in the level of assistance provided to

high-cost LECs and collected from interstate carriers and ratepayers.

22. We request comment upon the utility and advisability of adopting a permanent indexed cap on high-cost assistance. A cap would prevent sudden, large increases in the level of high-cost assistance. At the same time, we believe that the amount of high-cost assistance should be allowed to grow moderately over time if needed to promote universal service effectively. Accordingly, we do not intend to propose freezing the level of assistance but, instead, seek comment evaluating the merits of various potential indexing factors.

23. In our Interim Order, we temporarily indexed growth in the capped USF to the percentage of growth in the total number of access lines nationwide. As we indicated, that rate of growth has been relatively stable and moderate over the past few years. If the level of high-cost assistance were permanently indexed to the rate of growth in total access lines, it appears that a steady, stable, and moderate rate of growth in high-cost assistance would be likely. Accordingly, we seek comment on the use of the rate of growth in total access lines as a longer-term index factor for growth in high-cost assistance.

24. We also seek comment on indexing growth in total high-cost assistance to an inflation-based factor. Our decision, earlier in these proceedings, not to freeze the total level of the USF was based upon the Joint Board's belief that a total freeze "would effectively decrease the amount of assistance over time due to inflation."[19] If total high-cost assistance were indexed to an inflation-based factor, similar to the operation of price caps, we could avoid the problem anticipated by the Joint Board.

25. Finally, we also invite commenting parties to propose other index factors that may ensure moderate growth in the level of high-cost assistance. We ask that commenters evaluate proposed index factors in terms of their verifiability, susceptibility to manipulation, stability over time, ability to ensure adequate support for universal service, and potential effect upon the annual rate of growth in total high-cost assistance.

B. High-Cost Assistance Based Upon Actual Costs

26. Our current LEC assistance mechanisms are based upon the actual reported costs of LECs. As we discuss in Section IV.C. of this Notice, this use of actual reported costs does not provide a direct incentive for carriers to reduce or minimize their costs, and for that reason we invite comment on the use of various proxy factor approaches to replace the current assistance mechanisms.

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[19] 1984 Retargeting Recommendation, 49 Fed.Reg. at 48336, ¶58.

While the proxy approach appears promising, it may be difficult to identify proxy factors that correlate sufficiently with high-cost operations. In addition, even assuming that reliable proxy factors can be identified, many high-cost service providers may not fit the high-cost profile derived from the proxy factors. For these reasons, we are unwilling to dismiss the use of actual costs without further evaluation. We therefore request comment regarding several alternatives for revising the current assistance rules based upon reported costs.

1. Defining the Costs Used to Determine Assistance

27. Under our current LEC support mechanisms, loop costs and switching costs form the respective bases for USF and DEM weighting assistance. The USF provides high-cost assistance to both large and small LECs whose loop costs exceed the nationwide average by prescribed percentages. DEM weighting, based upon switching costs, provides interstate assistance to all small LECs, regardless of the level of their costs. The different structures of these two assistance mechanisms has provided an incentive for some LECs to miscategorize the costs associated with certain types of facilities. If the two assistance mechanisms were combined into one program applying a single standard for support, the existing incentive for miscategorization of costs could be removed. We therefore request comment upon the appropriateness and practicability of combining loop costs with switching costs to determine the amount of assistance to be provided to a high-cost carrier.

28. One potential problem with combining loop and switching costs to determine high-cost support is that a substantial portion of many LECs' switching costs is associated with the provision of toll service rather than local exchange services. Because high-cost assistance was intended to provide support for local services, it would be ideal to base support on costs related solely to the provision of local services. Including toll switching costs in the basis for a LEC's high-cost assistance may be inconsistent with the original goals of high-cost assistance.

29. In addition, basing high-cost assistance upon the combination of loop and switching costs may not be fair to some high-cost carriers. We currently base USF support on a company's total unseparated loop costs compared to the national average for such costs. If we retain that general structure for assistance but base support on a combination of loop and switching costs, carriers with a lower than average proportion of toll traffic may be disadvantaged. This could occur because the total cost per subscriber line for switching can vary significantly depending on the extent of a carrier's toll traffic operations. LECs that provide a large volume of toll service are likely to have very high unseparated switching costs. Those LECs' total loop and switching

costs per subscriber line thus are likely to be significantly greater than carriers that handle primarily local exchange traffic, and carriers with less toll investment per subscriber line thus could lose high-cost assistance, despite having extremely high costs associated with the provision of local service.[20]

30. Because high toll costs are not related to the provision of local service, we question whether they should be the subject of high-cost assistance. Therefore, we invite comment on whether we should exclude all, or a portion of, toll switching costs from any high-cost assistance mechanism that combines loop costs and switching costs. In raising this issue, we recognize that there is no established procedure for allocating switching costs between toll related services and other services. We believe that intrastate costs, especially if adjusted to remove toll switching costs as discussed above, may be a reasonable surrogate for "local" costs. We invite comment on whether we should prescribe a method for allocating between those two types of services and, if so, what method we might prescribe. We also invite comment on the criteria we might use to determine which toll switching costs should be excluded from high-cost assistance calculations in the event we decide that a portion of those costs should be excluded.

31. We are also concerned that it may be difficult to identify all costs associated with "local" traffic. For example, local traffic moves between central offices and accesses the public switched network by exchange trunks, and host remote trunks carry local traffic between remote switches and central offices. The costs associated with these local trunks would not, however, be classified as "local" costs using the existing Part 36 categories. Accordingly, we request comment on whether the costs of exchange trunks and host remote trunks should also be included in the definition of "local" costs.

32. We ask interested parties to propose a definition of eligible costs that is fair and practicable to administer. We ask, in particular, whether the increased complexity of a methodology that excludes toll switching costs while including all identifiable local service costs would be justified by its benefits.

33. Finally, we wish to consider the exclusion of certain types of costs from the data used to calculate the amount of a carrier's high-cost assistance. Specifically, we invite comment on whether we should remove general support expenses, executive and planning expenses, and general and administrative

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[20]This methodology has not had the same problem when based upon local loop costs because the same basic factor (25 percent) for allocating loop costs to local service is used for all LECs.

expenses from the basis for high-cost assistance.[21] A high level of these costs may chiefly reflect managerial and administrative decisions rather than an inherently high cost of providing telephone service. For that reason, we ask interested parties to address the appropriateness of excluding these costs from the cost basis for receipt of high-cost assistance.

2. Modifying the Current High-Cost Assistance Mechanisms

34. In this Notice, we invite comment on a number of alternative high-cost assistance mechanisms. Some of those alternatives would markedly depart from the structure of our existing rules. We are, however, also interested in considering modifications to the existing support mechanisms, in light of several years of experience with the current rules, to target more effectively the highest cost LECs that are in greatest need of assistance.

a. Reevaluate Assistance to Large LECs or Non-Rural Areas.

35. Throughout this proceeding, we and the Joint Board have repeatedly determined that small telephone companies, particularly those serving rural areas, have greater need of high-cost assistance than the larger LECs. In fact, we have twice retargeted the USF by decreasing assistance to large study areas.[22] In its 1987 Retargeting Recommendation, the Joint Board noted the projections of four LEC trade associations that the retargeting measures recommended by the Joint Board would "increase from 53% to 83% the proportionate share of high cost fund assistance paid to LECs with less than 200,000 lines."[23]

36. Setting 200,000 loops as the outer limit for "small" study areas has, however, still directed a sizable portion of the USF toward several of the largest LEC holding companies. In 1993, study areas owned by six of the eight largest LEC holding

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[21] See 47 C.F.R. §§ 36.621, 32.6120, 32.6710, and 32.6720 (1993).

[22] See 1984 Retargeting Recommendation, 49 Fed.Reg. at 48335, ¶56 ("additional assistance is necessary for small companies"); 1984 Retargeting Order, 50 Fed.Reg. at 942, ¶14 ("high cost assistance [should be] targeted to recognize the special situation of customers served by smaller, rural telephone companies"); and 1987 Retargeting Recommendation, 2 FCC Rcd at 2334, ¶86 ("small companies [are] most in need of assistance").

[23] The four trade associations making these projections were the National Rural Telephone Association, the National Telephone Cooperative Association, the Organization for the Advancement and Protection of Small Telephone Companies, and the United States Telephone Association. See 1987 Retargeting Recommendation, 2 FCC Rcd at 2333, ¶75, and at 2351, n.23.

companies[24] received approximately $290 million in USF assistance -- more than forty percent of the total USF. Although the amount of the large LECs' assistance per loop per month is generally small,[25] the large number of loops owned by those carriers results in significant payments.

37. If the goals of high-cost assistance were expanded to include support for facilities modernization,[26] massive growth in the fund could result unless the high-cost support mechanisms are retargeted. Specifically, such retargeting is likely to focus assistance more narrowly upon the users and service providers with the greatest need for support. Previously in this proceeding, it has been proposed that "at some point the high cost fund should be modified to eliminate support for the high cost study areas of the large LECs."[27] In this Notice, we ask interested parties to comment upon the extent to which high-cost assistance to the largest LECs or to non-rural areas is essential to promote universal service, and to address measures that would focus assistance more narrowly upon small study areas and rural regions.

38. Eliminate or Revise High-Cost Assistance to LECs Serving Large Study Areas. We invite interested parties to discuss whether it would be practicable to reduce or eliminate high-cost assistance to certain categories of service providers or service areas without imperiling our universal service goals. Specifically, we request comment upon the elimination of high-cost assistance for large study areas, which generally are owned by the largest LEC holding companies. These are financially healthy enterprises whose resources dwarf those of most of the other recipient companies. The USF is a system of general assistance determined by an assessment of each LEC's need for support throughout each of its study areas. The current system assumes that study areas served by small LECs have a greater proportionate need for high-cost assistance than study areas served by large LECs. As the Joint Board concluded earlier in this proceeding, larger LECs (and larger study areas) appear to have more flexibility than small companies in dealing with above-average

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[24]These companies include five of the seven Regional Bell Operating Companies ("RBOCs") (all except Ameritech and Pacific Telesis) and GTE. GTE, whose combined operations make it the largest LEC, received $224 million, more than one-third of the total fund, in 1993.

[25]For 1993, these payments average approximately 66 cents per loop per month. See Universal Service Fund 1992 Submission of 1991 Study Results by the National Exchange Carrier Association, Inc., CC Docket No. 80-286 (filed October 1, 1992).

[26]See Section III., supra.

[27]1987 Retargeting Recommendation, 2 FCC Rcd at 2333, ¶79, characterizing comments of Ameritech.

costs. We are, however, concerned that limiting high-cost assistance to small LECs or small study areas might reduce the large LECs' incentives to modernize, or even to continue to operate, high-cost exchanges. We are also concerned that the elimination of assistance for larger LECs could limit their ability to respond as competition develops in their local service areas.

39. We seek comment on eliminating assistance to large study areas. In addition, we request specific comment regarding the appropriate number of loops to use in defining eligibility for high-cost assistance in the event we take that step. One possibility would be to use 200,000 loops, already a distinguishing standard in our USF rules, as the cut-off point for assistance. We note, however, the Joint Board's opinion, in setting the standards for DEM weighting, that "a carrier with 50,000 to 200,000 loops does not qualify as a small carrier."[28] We therefore request that interested parties comment upon setting the limit at 50,000 or 100,000 loops.

40. If assistance to large study areas were to be eliminated, we ask commenters to propose an appropriate cut-off point if a sliding scale of assistance is adopted, as discussed in subsection IV.B.2.b., infra. If we adopt a sliding scale, it may be necessary to raise slightly the number of loops used as the cut-off point for assistance, in order to ensure that the percentage of assistance does not decline too rapidly for small LECs. Nonetheless, we believe that raising the cut-off point too high might defeat the purpose of eliminating high-cost assistance to large study areas. We seek comment on this analysis.

41. A variation on eliminating assistance to large study areas would be to eliminate high-cost assistance to price cap LECs. One rationale for such a delineation is that these carriers, like large study areas, are generally subsidiaries of large LEC holding companies with substantial resources or that may be able to maintain rates in high-cost areas at reasonable levels through internal subsidy mechanisms. In addition, this approach appears consistent with a price cap system of incentive regulation which encourages LECs to reduce costs. On the other hand, limiting high-cost assistance to non-price cap carriers could have the undesirable effect of discouraging LECs from electing price cap regulatory treatment. Moreover, this approach could exacerbate any existing incentives for price cap LECs to cease to operate high-cost exchanges. We request comment on this approach and, in addition, we invite interested parties to propose an effective means of eliminating or reducing support to LECs serving large study areas.

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[28]Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 2 FCC Rcd 2551, 2560 at ¶56 (1987) (1987 DEM Recommendation).

42. Eliminate Assistance to Non-Rural Areas. When we first implemented USF assistance, we expressed concern that reasonably-priced local service remain available in rural areas, which frequently have higher costs than more populous service areas. Instead of targeting assistance to rural areas, however, we adopted a system that compares average costs within each study area to the nationwide average, and then allots assistance on the basis of loops. One consequence of this approach is that a large portion of current USF assistance is provided to study areas composed of both rural and non-rural areas.

43. In reply comments submitted in response to our Interim Notice, US West proposed that USF assistance be retargeted so that it is available only in those exchanges where the preservation and expansion of universal service is in real jeopardy.[29] US West argues that universal service is not a concern in urban and suburban areas but that companies serving those areas can, under the current rules, receive USF assistance to fund advanced facilities deployment, such as fiber to the curb. US West also contends that competitive entry has occurred, or will soon begin, in urban and suburban telecommunications markets, and that providing USF assistance to only one participant--the LEC--is not conducive to further competitive development.

44. We request comment on whether we should target high-cost assistance only to rural areas where the cost of service is frequently high and where competitive entry may be less likely in the near future. One of the proposals suggested by US West in its reply comments is to target high-cost assistance to loops outside Metropolitan Statistical Areas ("MSAs"). We invite interested parties to comment on that approach, as well as a modified version, which would eliminate high-cost assistance to recipients within MSAs that exceed a specific population level. The modified version would allow some support for non-rural areas but would not assist the most densely populated areas where lower costs and competitive entry are likely. Commenters should address the effectiveness of these methods in targeting geographic areas most in need of high-cost assistance and the practicability of an MSA-based approach. In addition, commenters supporting the modified version should propose an upper population limit beyond which an MSA would not be eligible for assistance.

b. Establish a Sliding Scale of Declining Assistance.

45. As we have already noted, under our current USF rules study areas with fewer than 200,000 loops may allocate a greater percentage of their qualifying loop costs to the USF than those study areas with more than 200,000 loops. This sharp line of

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[29] See US West Reply Comments, CC Docket No. 80-286 at 3-6 (submitted October 18, 1993).

demarcation has drawn a significant amount of criticism. Critics have charged that our rules could cause study areas of similar size to receive radically different payments from the USF. For example, under our current rules, for a study area with an average loop cost that is 145 percent of the nationwide average, the USF assistance factor would be 65 percent if the study area had 199,000 loops but would be only 10 percent if the study area had 201,000 loops.

46. In addition, our existing high-cost assistance rules for study areas with 200,000 or fewer loops may undermine those carriers' incentives to invest and operate efficiently. Those small carriers currently allocate 90 to 100 percent of their incremental loop costs (above the threshold for assistance) to the interstate jurisdiction.[30] While a number of the smallest, highest cost LECs may require that degree of assistance, affording these levels of interstate allocation to all high-cost study areas with 200,000 or fewer loops provides no incentive to avoid or reduce excessive costs. A sliding scale of assistance could remedy that problem in an equitable manner, by maintaining the smallest, highest cost study areas near their current percentage of high-cost assistance and gradually decreasing the percentage of assistance for larger study areas.

47. In the preceding section, we have invited comment on eliminating assistance to study areas having more than a specified number of loops. We believe that our high-cost assistance mechanisms might function more smoothly and fairly if the different treatment of study areas based on number of loops were accomplished gradually. For that reason, we also invite comment on the desirability of a sliding scale of assistance, whereby the smallest carriers have the highest USF allocation factor, with that factor declining gradually based on the size of the study area. The sliding scale would provide high-cost assistance at some maximum percentage factor for the smallest study area and would decline on a linear basis to zero assistance at the cut-off point for study area size (based on the number of loops).[31]

48. We seek comment on the appropriate number of loops per study area to use as a cut-off point for receipt of high-cost

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[30]For their costs per loop, as defined in 47 C.F.R. § 36.621 (1993), that are between 115 and 150 percent of the national average, the high-cost factor is 65 percent. Added to the basic allocation factor of 25 percent, the total interstate allocation of those incremental loop costs is 90 percent. At 150 percent of the national average, the high-cost factor rises to 75 percent, for a total interstate allocation of those incremental loop costs (above 150 percent of the national average) of 100 percent. See 47 C.F.R. §§ 36.631 and 36.154 (1993).

[31]At that point, without a high-cost factor, the basic interstate allocation factor for NTS exchange plant costs would be 25 percent, the allocation factor for carriers that do not qualify for assistance. 47 C.F.R. §36.154 (1993).

assistance. We specifically ask parties to address the use of 200,000 loops, the current point of differentiation between large and small study areas, as the point at which assistance is eliminated. We also request comment regarding other cut-off points, both less than or greater than 200,000 loops.[32] Finally, we ask interested parties to propose an appropriate percentage for the maximum high-cost assistance factor to be used for the recipients with the fewest loops.[33]

c. Reevaluate the Percentage of Assistance for Above-Average Costs.

49. Assuming that we do not adopt a sliding scale, as we suggested in the preceding section, we request comment upon changing the percentage of interstate assistance for carriers with average loop costs above the threshold for assistance. Under the current USF assistance rules, LEC study areas with fewer than 200,000 lines may allocate 65 or 75 percent of their high costs (i.e., loop costs[34] above the threshold for assistance) to the interstate jurisdiction. With the basic interstate allocation of 25 percent, those recipients are able to allocate 90 or 100 percent of their incremental loop costs to the interstate jurisdiction.

50. We are concerned that LECs allocating a high percentage of their incremental loop investment to interstate operations may have little incentive to avoid costs that are not justified by sufficient customer demand or other economic need. While it is important to provide high-cost support sufficient to maintain the nationwide availability of reasonably priced local telecommunications service, support levels that are too high may provide no incentive for efficient investment and operation. We therefore request interested parties to comment upon whether the current high-cost factors have stimulated such financial practices by recipients of assistance and, if so, whether the high-cost factors should be reduced for some or all recipients.

d. Change the Threshold for USF Assistance.

51. Since initial implementation of the USF in 1986, the number of USF assistance recipients has grown dramatically. Even more significant, LECs are receiving USF assistance for an increasing percentage of loops and study areas as well. When USF

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[32]For example, the cut-off point could be reduced to 50,000 or 100,000 loops, or increased to 300,000 loops.

[33]The current maximum factors are 65 percent for costs per loop between 115 and 150 percent of the national average loop cost and 75 percent for costs in excess of 150 percent of the national average loop cost. 47 C.F.R. § 36.631 (1993).

[34]47 C.F.R. § 36.621 (1993).

support began in 1986, USF recipients received assistance on the basis of 19.5 million loops, approximately 18 percent of all loops.[35] By 1993, LECs were receiving USF assistance for 36.5 million loops, or nearly 27 percent of the nationwide total number of loops.[36] Similarly, the percentage of study areas receiving USF assistance has grown from 66 percent in 1986 to 78 percent in 1993. This expansion in the base of USF recipients has, correspondingly, increased the total amount of USF support.

52. We believe that high-cost support should be targeted toward those companies, and their subscribers, that are in significant need of assistance in order to fulfill our universal service goals. We also believe that USF assistance should not be a routine source of revenue for a large majority of LEC study areas. Moreover, the large percentage of LEC study areas receiving assistance tends to undermine our 1984 decision to adopt a basic allocation factor for jurisdictional separation of NTS costs. We believe that further expansion in the base of USF recipients could be limited by adjusting the threshold for qualifying to receive USF assistance. We therefore request comment regarding two alternatives for adjusting the threshold for assistance. We also request comment on the general issue of whether permitting an expanding base of USF recipients is in the public interest. We ask that commenting parties address the appropriate percentage of loops and study areas to receive USF assistance.

53. Raise the Threshold for Receiving High-Cost Assistance. At present, for a LEC study area to receive USF support, its average loop cost must be at least 115 percent of the nationwide average loop cost per working loop.[37] The current threshold, which allows nearly 80 percent of all study areas to receive some level of assistance, may be lower than is necessary to meet our universal service goals. Moreover, the costs per loop of many large carriers are close to the threshold. Thus, although the amount of assistance per loop directed to those carriers may be relatively small, the total amount of assistance provided to them is large due to the large number of loops within their study areas.

54. If the basic structure of the current USF high-cost assistance mechanism is retained, we could raise the threshold for receiving high-cost assistance perhaps to 130 percent. Raising the threshold would maintain support for extremely high-cost carriers most in need of assistance, while eliminating assistance to carriers with costs relatively close to the national average.

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[35]USF assistance in 1986 was based on 1984 data, when the total number of loops was 111 million.

[36]The nationwide total number of loops in 1993 was 137 million.

[37]See 47 C.F.R. § 36.631 (1993).

Moreover, if the Commission were to expand the goals of high-cost assistance, this adjustment could still make support available for modernization and technological improvements in the highest cost areas without significantly raising the total amount of assistance. We ask for comment upon this approach.

55. Adjust the Threshold to Reflect Relative Deviation from the Nationwide Average. Rather than simply raising the qualifying threshold to some fixed amount, we could, instead, develop a threshold based on accepted statistical methods that would be adjusted as the dispersion characteristics of LECs' costs per loop change relative to the national average. One such possibility is to set the qualifying threshold for USF assistance at the national average cost per loop plus one "standard deviation" or some fraction of one standard deviation of LEC costs per loop.[38]

56. Setting the threshold for assistance on the basis of standard deviation from the mean would directly address changes in the dispersion characteristics of LEC costs per loop. Adjustment of the threshold using this method thus could prevent or mitigate continuing expansion in the percentage of loops or study areas receiving assistance.[39] For the same reason, this method would likely moderate growth in total high-cost assistance while continuing to support the highest cost LECs.[40] LECs with very high costs per loop would be affected only slightly, and only those LECs whose costs per loop are close to the current threshold would experience a significant change in the level of assistance received. We ask for comment on this method of establishing the annual threshold for USF assistance.

e. Reevaluate DEM Weighting.

57. In Section IV.B.1. of this Notice, we invite comment on including switching costs within the costs that form the basis for high-cost assistance. If this approach were adopted, it could replace the current DEM weighting assistance mechanism for small LECs. We invite comment upon the advantages and disadvantages of combining the current USF and DEM weighting assistance programs into a single form of high-cost support.

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[38]The standard deviation is a frequently-used statistical measure of the dispersion or variability of a set of numbers.

[39]Because the national average cost per loop is weighted based on the number of loops in each study area, the standard deviation would also be weighted based on the number of loops.

[40]If the current rules were modified to reflect this approach, in 1994 high-cost assistance would be provided to carriers with average costs per loop above approximately 129 percent of the nationwide average.

58. We also ask commenters to discuss whether we need to continue DEM weighting, even in the event that USF assistance continues to be based solely upon loop costs. Specifically, we ask that interested parties address the question of whether high-cost study areas typically experience much higher than average switching costs as well as loop costs. If that is not the case, we request comment upon whether DEM weighting assistance should be eliminated or revised, and what effects, if any, could be expected to follow from such changes.

C. High-Cost Assistance Based Upon Proxy Factors

59. High-cost assistance mechanisms based upon actual costs do not encourage cost reduction or minimization, because they allow recipients to obtain additional assistance when they incur additional costs. Under the current USF rules, as discussed in Section IV.B.2.c., recipient LEC study areas with 200,000 or fewer lines currently allocate 90 to 100 percent of their above-threshold incremental loop costs to the interstate jurisdiction.[41] Because the USF is defined by aggregating the qualifying costs of hundreds of separate recipient study areas, our ability to examine the underlying costs for all of those companies is clearly limited. Consequently, there is a relative lack of accountability in this system of assistance which, because it is based upon actual reported costs, does not discourage unnecessary expenditures. Moreover, because high-cost assistance is based on only certain categories of costs, our rules may influence unduly carriers' investment decisions and categorization practices. Finally, a cost-based assistance program that differentiates between large and small study areas could create an artificial incentive for large LECs to cease to operate their high-cost exchanges.

60. As we reexamine the goals of high-cost assistance, the costs associated with new investment cannot be ignored in evaluating the current assistance mechanisms and, if necessary, in designing new methods. It is imperative that investments to improve and enhance the telecommunications infrastructure impose only necessary costs upon all segments of the telecommunications industry. Such efficiency is particularly important with respect to the existing system of high-cost assistance, because the new investments of high-cost assistance recipients will be funded, at least in substantial part, by other telecommunications carriers and their subscribers. Imposing excessive costs on other segments of the industry could inflate unnecessarily rates for those services. Accordingly, we believe that it is important to examine alternative bases for assistance that would encourage support recipients to control their costs of providing service, thereby minimizing the costs imposed upon other telecommunications users.

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[41]This allocation includes the 25 percent basic allocation factor plus 65 or 75 percent USF high-cost allocation factors.

61. Consistent with our goal of properly targeting assistance to high-cost companies while promoting efficient investment and operation, we wish to examine alternatives that would base assistance on the application of relevant proxy factors. In essence, this approach would determine each recipient's assistance on the basis of the reasonable costs per loop for carriers with certain characteristics, rather than on the basis of the recipient's actual reported costs. A recipient's amount of high-cost assistance thus would reflect the difference between its projected reasonable cost per loop, as established by the proxy factors, and the nationwide average cost per loop. Basing a recipient's assistance on the projected reasonable cost to serve high-cost areas could replace the current rewards for excessive costs with an incentive for recipients to curb costs. In addition, if properly structured, a proxy approach would have the advantage of calculating assistance based upon readily available and verifiable information.

62. At earlier stages of this proceeding, we raised the issue of using proxy or surrogate factors to apportion USF assistance. Although we have declined in the past to use cost surrogate factors, we believe that the time has arrived to explore this alternative in greater depth. A properly designed proxy approach could promote infrastructure development and ensure adequate support for high-cost areas while deterring inefficient expenditures.

63. A reasonable method for calculating assistance on the basis of proxy factors should rely on a limited number of relevant and readily verifiable factors. Many characteristics previously proposed as proxy factors appear either too difficult to verify, insufficiently correlated with high costs, or both. For example, a system that attempted to classify and assign weight to various types of terrain based upon the projected cost of providing service would be extremely difficult to design and verify. Local rate levels, for a variety of reasons, may not correlate adequately with high cost of service and could raise complex issues relating to the size and definition of local calling areas.[42] Using average length of loop or subscriber density per loop mile might not be sufficiently susceptible to verification, even if it could be demonstrated that either or both of those factors correlate significantly with cost of service information. We therefore do not at this time set forth a specific proxy methodology that incorporates any of the foregoing factors. Nonetheless, we request comment on whether and, if so, how those factors might be included in a proxy methodology.

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[42] See 1987 Retargeting Recommendation, 2 FCC Rcd at 2334, ¶88.

64. The proxy methodologies on which we now invite comment involve the use of factors that demonstrate reasonable correlation with cost levels or the need for high-cost assistance. In addition, the factors appear easier to verify than most other potential proxy factors. We seek comment on the proxy methods described below. In addition, we request comment upon the suitability of a proxy approach for accomplishing our universal service goals. Finally, we ask that commenting parties propose additional alternatives for appropriate proxy methodologies.

1. Determine USF Assistance Using a Formula Similar to NECA's Methodology for Determining USF Assistance to Average Schedule LECs.

65. LECs whose costs are recovered based on average schedule rates currently receive USF assistance based on a formula whose only independent variable is the number of loops per exchange. This formula is developed annually by NECA and is derived from data provided by the cost-based LECs. This type of formula essentially uses exchange size as a proxy factor for cost per loop. Applying such a formula to all LECs would provide assistance based upon the average cost per loop for LECs with similar average exchange sizes. Because recipients would not receive a fixed percentage of assistance for every dollar spent, they would not be rewarded for incurring additional costs. The formula thus would introduce an incentive for cost control that does not exist under the current USF rules. We seek comment on this approach.

2. Determine USF Assistance Using LEC Study Area Size and Population Density as Proxy Factors.

66. Throughout this proceeding, the Joint Board and this Commission have consistently found that LEC study areas with a relatively small number of loops, particularly in rural areas, have greater need for high-cost assistance than larger LECs. Therefore, we invite comment on whether we should take study area size and general population density into account in determining USF assistance. Both study area size and population density may be verified from objective sources. In addition, we believe that population density would display a reasonable degree of correlation with high loop costs.

67. This methodology would involve projecting expected cost per loop on the basis of study area size (i.e., number of loops) and population density. We seek comment on whether using the number of loops as one factor in projecting expected cost per loop would reflect the additional costs associated with small company study areas. Similarly, we seek comment on whether adjusting for the effects of population density would address the special needs of sparsely populated rural areas.

68. This proxy approach, like the first approach, would appear to promote efficiency by abolishing the link between increased expenditures and increased assistance. We seek comment upon this approach for using study area size and population density as proxy factors in establishing the basis for determining USF assistance. We request, in particular, analysis of the extent to which the results under this method could be expected to vary from the results using NECA's current formula for average schedule companies, and the reasons for such variances. In addition, we request proposals for the development of a suitable formula, incorporating these two factors, for calculating high-cost assistance.

3. Combine a Proxy Factor for Cost and a Proxy Factor for General Need In Determining Assistance.

69. One of the original goals of high-cost assistance was to assure that local rates in high-cost areas do not greatly exceed rates in other areas of the country. Nonetheless, variations throughout the country in average income levels and in the cost of living cause corresponding differences in the general affordability of local telephone service. Simply put, the affordability of local telephone service in a given area of the country is likely to be affected by the disposable income of telecommunications consumers in that area. For that reason, the same local rate level may have profoundly different effects upon universal service in different locations, depending on the economic conditions of each area.

70. The third proxy method on which we invite comment would incorporate both a proxy for cost and a proxy for the general economic need of subscribers in a given study area. The proxy factor for cost could include either the elements of the first or second proxy method, as described above.[43] A study area's proxy factor for general need would reflect the average disposable income of individuals within a designated geographic area. Using that approach, areas with extremely low average income levels, or extremely high costs of living, or both, would have a higher proxy factor for general need than areas with average income and cost of living close to the national average. One way of computing disposable income could consist of calculating a ratio of average income to the cost of living. We ask interested parties to comment upon this means of assessing disposable income and to propose alternative methodologies for evaluating average disposable income or other indicia of the general economic need for assistance.

71. We also seek general comment upon this proxy factor method for determining assistance, which would reflect both the expected cost of service and the general economic status of persons

[43] See ¶¶65-68, supra.

living in each recipient study area. In particular, we ask interested parties to comment upon whether the additional complexity of such a system would be justified by greater fairness in the disbursement of high-cost assistance. Finally, we request that interested parties propose a formula containing factors based on the approach to high-cost assistance outlined in this section.

D. Use Proxy Factors to Make an Initial Determination of the Amount of High-Cost Assistance To Be Directed to Each State Jurisdiction.

72. We also request comment upon a method that would use, as a first step, a proxy formula to distribute a predetermined amount of assistance among the state jurisdictions. The nationwide total assistance could, if desired, be allowed to grow at an indexed rate. The proxy formula would be used to determine the percentage of total assistance allocated to each jurisdiction. The proxy formula used to allocate total assistance among the state jurisdictions could be derived from one of the proxy factor alternatives discussed in section IV.C. The amount of assistance directed toward carriers in a given state would reflect both the proxy factors (for example, the combination of a cost proxy -- such as population density -- and a general need proxy) as well as the total number of subscribers within the state.

73. Once the amount of assistance to be directed to each state jurisdiction has been established, the second step would involve determination of the amount of support for each individual recipient, depending upon the carrier's actual reported costs. This method could increase accountability, because most state assistance "pools" would consist of fewer than fifty study areas. At the same time, this alternative would appear to address the concerns raised by Vermont in its petition for waiver,[44] because it would focus upon the general needs and characteristics of the state as a whole, without distinguishing between large and small carriers. In the paragraphs that follow, we invite comment on three alternative means of distributing high-cost assistance following allocations to state jurisdictions on the basis of proxy factors.

74. After Allocating High-Cost Assistance Among State Jurisdictions Based Upon Proxy Factors, Use Actual Reported Costs to Determine the Distributions to Individual Carriers. As we explained earlier in this Notice, there are differing advantages to the use of proxy factors and the use of actual reported costs to determine high-cost assistance. Proxy factors are intended to promote efficient investment and operation, but could deny

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[44] See Waiver of Section 36.631 of the Commission's Rules Governing the Universal Service Fund, 8 FCC Rcd 7588 (1993).

assistance to individual high-cost carriers that do not meet the profile for assistance that forms the basis for the proxy factors.

75. In light of the respective advantages and disadvantages of using actual costs or proxy factors to distribute high-cost assistance, we wish to consider using a "mixed" method that would rely on one or more proxy factors to determine the total amount of high-cost assistance provided to each jurisdiction and then allocate that fixed sum on the basis of recipients' actual costs.[45] We believe that this method could fairly distribute assistance among the various jurisdictions and, moreover, could promote accountability due to the interrelationship between the assistance provided to carriers within a single jurisdiction. We request comment upon this approach for determining high-cost assistance.

76. Allow Each State Commission to Establish Standards for Distributing High-Cost Assistance to the Carriers Within Its Jurisdiction. Another possible method would allow each state utility commission to administer the distribution of its state's high-cost assistance allocation. Allocations to the state jurisdictions would be determined by proxy factors, and the state utility commission would determine allocations from the state's high-cost assistance fund to individual carriers. State administration, under general guidelines promulgated by this Commission, could allow some variation among the distribution formulae used in various states, and thus could reflect cost characteristics unique to each state.

77. An advantage of this system is that a state commission is aware of the local service providers' network capabilities and the needs of the various communities within its jurisdiction. A state commission thus could adapt the general guidelines for high-cost assistance in order to serve the goals of universal service most effectively. We request comment upon state commission administration of distributing high-cost assistance to individual carriers.

E. Establish a Voucher or Credit System for Telecommunications Users.

78. We invite interested parties to address the possibility of establishing a system whereby telecommunications users can claim high-cost assistance credits on their local service bills. We believe that this approach could eliminate any competitive advantage which the current rules afford traditional

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[45]The threshold for assistance could vary among jurisdictions, because the threshold would need to be adjusted so that the total support provided to carriers within the state would be equal to the available funds allocated to the jurisdiction using proxy factors.

LECs. Proponents of such a system claim that the near future will see increasing competitive entry into local service markets, but that the existing high-cost assistance mechanisms may impede full and fair competition by giving the established LECs financial support denied to their competitors. Opponents claim that established LECs are the service providers of last resort and that, therefore, allowing credits to be used for service from competitors who are not required to offer ubiquitous service would be unfair, because the highest cost areas within a region would be left for the LEC to serve. We invite comment on this issue.

79. Given the likelihood of significantly expanding local service competition in the foreseeable future, we believe it prudent to consider replacing the existing high-cost assistance mechanisms with a system, based upon customer credits, that does not discriminate among providers of local telecommunications services. We request comment upon a two-step method for implementing a customer voucher system. The first step of this method would involve allocating high-cost assistance among state jurisdictions based upon proxy factors. After the nationwide high-cost assistance total is allocated among the states, the second step would require a determination regarding the amount of the credit or voucher available to customers in various locations within a state. We seek comment on this approach.

80. We also request that interested parties propose other alternatives for a voucher system that would encourage competition and decrease unnecessary subsidies while maintaining adequate support for customers and carriers needing assistance. In addition, we ask for specific comment upon the following issues: whether the amount of the customer credit should be uniform within each state jurisdiction, or whether it should vary based upon the needs of individual users or communities; and if the latter, what standards should be used in determining the amount of high-cost assistance credit. We seek comment upon the difficulty of administering a system affording credits to individual users. Finally, we request that interested parties comment upon whether customer vouchers should be available for all types of local services[46] and, in addition, project the effect of such a system upon competition among established LEC service providers and prospective competitors.

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[46]In other words, should telecommunications users be able to apply their vouchers or credits to every local telecommunications service, such as cellular telephone service, personal communications service, competitive access service, and other forms of local telecommunications that are now or may eventually be offered to consumers.

F. Need for Transition Mechanisms.

81. Many of the proposals for high-cost assistance contained in this Notice differ significantly from the present USF high-cost assistance mechanisms. While our goal is to improve the existing system of support for high-cost carriers, we are also mindful of the potentially disruptive effect upon individual LECs of implementing significant changes in either USF assistance or DEM weighting.

82. We invite comment upon the need for a transition period for gradually eliminating the current assistance mechanisms and gradually introducing any modifications or replacement mechanisms. We also request that interested parties propose an appropriate length of time for the transition process as well as the best means of accomplishing the transition with a minimum disruptive effect upon current recipients.

V. PROCEDURAL MATTERS

A. Ex Parte

83. This proceeding is exempt from ex parte restraints or disclosure requirements, as provided in Section 1.1204 of our rules.[47]

B. Comment Dates

84. We invite comment on the alternatives set forth above. Interested parties must file initial comments on or before October 28, 1994, and reply comments on or before December 2, 1994. To file formally in this proceeding, interested parties must file an original and four copies of all comments. If interested parties want each Commissioner to receive a personal copy of their comments, they must file an original plus nine copies.

85. Interested parties should send comments to: Office of the Secretary, Federal Communications Commission, Washington, D.C. 20554. Parties should also file one copy of any documents filed in this docket with the Commission's copy contractor, International Transcription Services, Room 640, 1990 M Street, N.W., Washington, D.C. 20036. We also ask that parties send a copy of their comments to each member of the Federal State Joint Board and its staff, as indicated in the attached service list. Comments will be available for public inspection during regular business hours in the FCC Reference Center (Room 239) of the Federal Communications Commission, 1919 M Street, N.W., Washington, D.C. 20554. For further information contact Deborah Dupont at (202) 418-0873.

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[47] 47 C.F.R. section 1.1204 (1993).

VI. ORDERING CLAUSE

86. Accordingly, IT IS ORDERED that, pursuant to Sections 1, 4(i), 4(j), 403, and 410(c) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 154(j), 403, and 410(c), an inquiry IS COMMENCED concerning possible proposals to change Part 36 of the Commission's Rules, 47 C.F.R. Part 36, as described above.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

APPENDIX: HISTORY OF THE UNIVERSAL SERVICE FUND AND DEM WEIGHTING

I. The Universal Service Fund

1. The concept behind establishment of the USF arose in 1982, as an outgrowth of proposed revisions to the jurisdictional separation of non-traffic sensitive ("NTS") exchange plant costs.[1] The subscriber plant factor ("SPF"), the usage-based factor then used to allocate NTS costs between the interstate and intrastate jurisdictions, was causing increasing percentages of those costs to be allocated to interstate operations. Because NTS costs are not incurred on a usage-sensitive basis, we wished to consider replacing SPF with fixed allocation factors.

2. The Joint Board Staff (the Staff) urged that the successor to SPF be designed to reflect "the special needs of high cost areas,"[2] many of which had high interstate allocations under SPF. The Staff believed that without such adjustments for high-cost companies, those LECs would experience major shifts of NTS costs to their intrastate operations, causing large increases in local telephone rates. We therefore proposed to replace SPF with three new factors: a basic allocation factor, a high-cost factor to provide assistance to areas with high costs, and a transition factor "to minimize dislocations caused by moving away from the existing SPF basis."[3]

3. In developing an appropriate replacement for SPF to allocate NTS local exchange plant, the Joint Board recommended "an equal percentage interstate allocation of NTS local exchange plant costs for all study areas in conjunction with appropriate protection for subscribers in high cost areas."[4] The Joint Board proposed, and we adopted,[5] the replacement of SPF with a 25 percent basic interstate allocation factor for NTS exchange plant costs. In addition, the Joint Board recommended the establishment of a banded high-cost support mechanism designed to provide a greater degree of assistance to LECs with the highest average NTS costs.

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[1]These NTS costs are primarily the costs associated with the exchange plant located between customer premises and the local switching office.

[2]Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 47 Fed.Reg. 54479, 54485 at ¶35 (December 3, 1982).

[3]Id. at ¶34.

[4]Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 48 Fed.Reg. 46556, 46584 at ¶38 (October 13, 1983) (1983 Recommendation).

[5]Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 96 F.C.C. 2d 781 (1984) (Initial USF Order).

The Joint Board suggested a transition period for phasing out SPF and phasing in the new basic allocation factor and high-cost factor.[6]

4. The Joint Board determined that a high-cost support mechanism would "help protect the nationwide availability of telephone service at reasonable rates while limiting the amount to be recovered through carrier's carrier access charges."[7] We found that the methodology recommended by the Joint Board represented "a sound balancing of concern for the promotion of universally available telephone service at reasonable rates and the need to prevent uneconomic bypass of the local exchange."[8] We therefore adopted the high-cost support mechanism recommended by the Joint Board.

5. Concurrently with proceedings in this docket to revise the jurisdictional separation of NTS exchange costs, we were considering the adoption of interstate exchange access charges. At that time, a great deal of concern was expressed regarding the effect of the federal subscriber line charge ("SLC") upon customers of small telephone companies. As a result, we decided to defer the effective date of the federal SLC while the Joint Board considered a means of "increasing the assistance that is provided to customers of small companies in high-cost areas through the Universal Service Fund."[9] After further proceedings in this docket,[10] the Joint Board recommended that we establish a two-tiered system of assistance, whereby USF assistance would be increased for LEC study areas with fewer than 50,000 loops and decreased for study areas with more than 50,000 loops.[11] We adopted the Joint Board's recommendation.[12]

6. In 1986, we undertook an examination of the "cohesive package" of SLCs, lifeline programs, and high-cost

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[6]1983 Recommendation, 48 Fed.Reg. at 46568-69, ¶¶68-69.

[7]Id. at ¶63.

[8]Initial USF Order, 96 F.C.C.2d at 794, ¶29.

[9]MTS and WATS Market Structure, 97 F.C.C.2d 834, 841 at ¶¶24-25 (1984) (Second Access Charge Reconsideration Order).

[10]Pursuant to a "Further Notice of Proposed Rulemaking," MTS and WATS Market Structure; and Amendment of the Commission's Rules and Establishment of a Joint Board, 49 Fed.Reg. 18318 (April 30, 1984) (1984 Further Notice).

[11]MTS and WATS Market Structure; and Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 49 Fed.Reg. 48325, 48335-36 at ¶56 (December 12, 1984) (1984 Retargeting Recommendation).

[12]MTS and WATS Market Structure; and Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 50 Fed.Reg. 939 (January 8, 1985) (1984 Retargeting Order).

assistance measures.[13] We asked commenting parties to evaluate the effects of those three mechanisms and to consider whether revisions were needed in order to preserve universal service, promote economic efficiency, eliminate service pricing discrimination, and deter uneconomic bypass. After considering the comments and proposals submitted in response to our 1986 Notice, the Joint Board recommended,[14] and we adopted,[15] a retargeting of the high-cost assistance measures provided to telephone companies with high-cost study areas. Assistance to study areas with fewer than 200,000 loops was increased while assistance to larger study areas was decreased.[16] The Joint Board's recommendation was premised upon an assumption that small companies have more need for assistance than larger LECs, which were believed to have greater flexibility in dealing with above-average costs.[17] There was also evidence that the retargeting of the high-cost measures would decrease the overall size of the USF significantly.[18]

7. Both the USF and the 25 percent basic allocation factor for NTS exchange plant costs were phased-in over a

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[13]MTS and WATS Market Structure; and Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, CC Dockets No. 78-72 and 80-286, Mimeo No. 5537 (July 2, 1986) at 8, ¶12 (1986 Notice). The 1986 Notice is summarized at 51 Fed.Reg. 27426 (July 31, 1986).

[14]MTS and WATS Market Structure; and Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 2 FCC Rcd 2324 (1987) (1987 Retargeting Recommendation).

[15]MTS and WATS Market Structure; and Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 2 FCC Rcd 2953 (1987) (1987 Retargeting Order).

[16]For study areas with 200,000 or fewer working loops, the additional interstate allocation is 65 percent of the unseparated cost per loop between 115 and 150 percent of the national average cost per loop, multiplied by the number of working loops; for the cost per loop that exceeds 150 percent of the national average cost per loop, the additional interstate allocation is 75 percent of the unseparated cost per loop multiplied by the number of working loops. For study areas with more than 200,000 working loops, the additional interstate allocation of unseparated loop costs is as follows: ten percent of such costs between 115 and 160 percent of the national average, thirty percent of such costs between 160 and 200 percent of the national average, sixty percent of such costs between 200 and 250 percent of the national average, and 75 percent of such costs in excess of 250 percent of the national average. 47 C.F.R. §36.631 (1993).

[17]1987 Retargeting Recommendation, 2 FCC Rcd at 2334, ¶86.

[18]Commenters supporting the change estimated that it would cause the USF to decrease from $448 million per year to $390 million per year. 1987 Retargeting Recommendation, 2 FCC Rcd at 2333, ¶75. See also 1987 Retargeting Order, 2 FCC Rcd at 2958, ¶36.

transition period lasting several years.[19] Over the transition period, the basic allocation factor, supplemented by the USF factor for high-cost study areas, gradually replaced SPF.[20] During 1993, the final year of the transition, both the 25 percent basic allocation factor and the USF assistance factor were at their full transition levels.

II. DEM Weighting

8. In our 1984 Further Notice proposing additional high-cost assistance for small telephone companies, we also asked the Joint Board to undertake a comprehensive review of the jurisdictional allocation of costs associated with central office equipment ("COE").[21] We asked the Joint Board to focus on the continuing validity of the existing jurisdictional allocation methods for COE, particularly the method used to apportion costs associated with local dial switches, in light of the "major technological and engineering changes in COE since the last in-depth study of separations procedures."[22] At that time, the cost of local dial switching equipment was split between traffic-sensitive ("TS") and NTS costs.[23] The TS portion of such costs was allocated between the interstate and intrastate jurisdictions on the basis of relative dial equipment minutes of usage ("DEM").[24] Toll DEM were then weighted for each office on the basis of a toll weighting factor intended to reflect, for the particular type of switching equipment, estimated cost differences per minute of use for toll and local usage.

9. In 1987, the Joint Board found that changing technology and the introduction of digital switching had made it hard to justify treating some local switching equipment costs as TS and others as NTS. The Joint Board therefore recommended that the distinction be eliminated and that the costs of local switching equipment be treated as TS and allocated between the jurisdictions

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[19]See 47 C.F.R. §§36.641 and 36.154(c)-(f) (1993). See also 47 C.F.R. §§67.641 and 67.124(d) (1986).

[20]SPF had previously been frozen at its 1981 level. See Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, FCC 81-565 (December 14, 1981) (1981 SPF Recommendation), and 89 F.C.C.2d 1 (1982) (1982 SPF Order).

[21]1984 Further Notice, 49 Fed.Reg. at 18319-20, ¶¶8-11.

[22]Id. at 18320, ¶9.

[23]Equipment is considered TS when its costs vary with usage and NTS when its costs do not vary with usage.

[24]Dial equipment minutes are the minutes of holding time of the originating and terminating local dial switching equipment.

on the basis of relative usage, using measured DEM. The Joint Board rejected the use of a DEM toll weighting factor, finding that "modern digital switching equipment has greatly reduced, if not eliminated, the additional cost of toll switching."[25] The Joint Board further proposed a five-year transition period beginning in 1988.

10. The Joint Board recommended, however, that assistance be provided to small study areas in order to offset potential cost shifts to intrastate operations triggered by the transition to DEM. The Joint Board's plan did not propose to include such assistance as part of the USF, but instead involved a separate means of assistance via weighting of the DEM factors for small companies. Depending on the number of their access lines, small study areas would be allowed to use a DEM weighting factor of 2.0, 2.5, or 3.0. Only study areas with 50,000 or fewer access lines were to be eligible to use the weighting factors, because the Joint Board determined that "a carrier with 50,000 to 200,000 subscriber loops does not qualify as a small carrier."[26]

11. We adopted the Joint Board's recommendations for the use of DEM to allocate local switching costs and for the establishment of DEM weighting factors in order to provide assistance to small companies.[27] We also approved the Joint Board's plan for a five-year transition to DEM weighting.[28] The last year of that transition period was 1992; therefore, as of 1993, DEM and the DEM weighting factors for small study areas were at their full transition level.

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[25]Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 2 FCC Rcd 2551, 2559 at ¶49 (1987) (1987 DEM Recommendation).

[26]Id. at 2560, ¶56.

[27]MTS and WATS Market Structure; and Amendment of Part 67 (New Part 36) of the Commission's Rules and Establishment of a Federal-State Joint Board, 2 FCC Rcd 2639 (1987) (1987 DEM Order).

[28]Id. See 47 C.F.R. §36.125(1993).

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Section 19 of the	)	
Cable Television Consumer Protection	)	
and Competition Act of 1992	)	CS Docket No. 94-48
	)	
Annual Assessment of the Status of	)	
Competition in the Market for the	)	
Delivery of Video Programming	)	

FIRST REPORT

Adopted: September 19, 1994 **Released: September 28, 1994**

By the Commission:

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I.
INTRODUCTION

1. Pursuant to the Cable Television Consumer Protection and Competition Act of 1992 (the "1992 Cable Act" or "the Act"),[1] the Commission is required to report to Congress annually "on the status of competition in the market for the delivery of video programming."[2] This report (the "*Report*" or the "*Competition Report*") is the first of these annual competition studies.[3]

A. Evolving View of Competition in the Market for the Delivery of Video Programming

2. In the ten years since Congress enacted the first major statute addressing the cable industry -- the Cable Communications Policy Act of 1984[4] -- the view of competition in the market for the delivery of video programming has evolved, both in Congress and at the Commission. As the Commission recognized in the report on competition in the cable television industry that it issued in 1990,[5] Congress enacted the 1984 Cable Act to encourage the growth of cable systems, the development of cable services and the provision of diverse

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[1] Pub. L. No. 102-385, 106 Stat. 1460 (amending the Communications Act of 1934 (the "Communications Act") and codified at 47 U.S.C. § 151, *et seq.*).

[2] Communications Act § 628(g), 47 U.S.C. § 548(g) (requiring the Commission to report to Congress "beginning not later than 18 months after promulgation of the regulations required by [Section 19(c) of the 1992 Cable Act]"). Those regulations were adopted on April 1, 1993. *Implementation of Sections 12 & 19 of the 1992 Cable Act -- Dev. of Competition & Diversity in Video Programming Dist. & Carriage, First Report & Order ("Program Access Report & Order")*, 8 FCC Rcd 3359 (1993), *recon. pending* MM Docket No. 92-265. Consequently, the *Report* is due on October 1, 1994.

[3] The Commission began this study with a notice of inquiry, which it released May 19, 1994. *Implementation of Section 19 of the 1992 Cable Act -- Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Notice of Inquiry*, 9 FCC Rcd 2896 (1994) ("*NOI*"). In response to the *NOI*, the Commission received comments and reply comments, some of which were not timely filed. In the interest of compiling as complete a record as possible, those late-filed pleadings are accepted and have been considered in this *Report*. The Commission also received numerous *ex parte* submissions, copies of which have been placed in the record. A list of those comments, reply comments and other submissions is set forth in Appendix A.

[4] Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2779 (codified as amended by 1992 Cable Act at 47 U.S.C. § 151, *et seq.*) (1984) ("1984 Cable Act" or "1984 Act").

[5] *Rate Deregulation & the Commission's Policies Relating to the Provision of Cable Television Serv., Report on Competition*, 5 FCC Rcd 4962 (1990) ("*1990 Cable Report*").

sources of information.[6] Accordingly, one of the primary purposes of the 1984 Cable Act was to "promote competition in cable communications and minimize unnecessary regulation that would impose an undue economic burden on cable systems."[7]

3. To fulfill this Congressional purpose, the 1984 Act imposed various limitations on the authority of local government entities to regulate cable services and, in particular, permitted regulation of basic cable rates only where, pursuant to Commission-established criteria, "a cable system is not subject to effective competition."[8] The Commission later determined that "effective competition" existed when at least three unduplicated broadcast television signals were "available" to the cable community.[9] In essence, that determination deregulated the rates of approximately ninety-seven percent of all cable franchises.[10]

4. The 1984 Cable Act was a success in many ways. The number of communities and homes served by cable grew dramatically, channel capacity increased, and new programming was created.[11] However, as the Commission found in its *1990 Cable Report*, there was little competitive constraint on cable market power after passage of the 1984 Act, and cable system operators were able to collect monopoly profits through the imposition of significant rate increases on subscribers.[12]

5. In response to those trends, Congress passed the 1992 Cable Act, which in essence, re-regulated the cable industry. In enacting the 1992 Cable Act, Congress found that "[t]he average monthly cable rate has increased almost 3 times as much as the Consumer Price Index ["CPI"] since rate deregulation [under the 1984 Cable Act]."[13] Congress also found that without competition, there was "undue market power for the cable operator as compared to that of consumers and video programmers," and that "the cable television industry has become a dominant nationwide video medium."[14] However, Congress

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[6] *Id.* ¶¶ 1-5, 5 FCC Rcd at 4964-68.

[7] Communications Act § 601(g), 47 U.S.C. § 521(6).

[8] 1992 Cable Act sec. 2, 106 Stat. at 1460.

[9] 47 C.F.R. § 76.33(a) (1985) (superseded).

[10] 1992 Cable Act, sec. 2(a)(1), 106 Stat. at 1460.

[11] H.R. REP. NO. 862, 102d Cong., 2d Sess. 56 (1992), *reprinted in* 1992 U.S.C.C.A.N. 1231, 1238; S. REP. NO. 92, 102d Cong., 1st Sess. 3 (1991), *reprinted in* 1992 U.S.C.C.A.N. 1133, 1135-36; *1990 Cable Report* ¶ 3, 5 FCC Rcd at 4966.

[12] *1990 Cable Report* ¶ 13, 5 FCC Rcd at 4972-73.

[13] 1992 Cable Act, sec. 2(a)(1), 106 Stat. at 1460.

[14] 1992 Cable Act secs. 2(a)(2-3), 106 Stat. at 1460.

specifically articulated as a central and critical goal of the legislation a "[p]reference for competition," as opposed to rate regulation of cable systems.[15] Accordingly, the 1992 Act generally provides that where a cable system is subject to effective competition, its rates shall not be subject to governmental regulation.[16]

6. As the Commission recognized in the *NOI*, the 1992 Cable Act's regulatory scheme serves as a "transitional mechanism until competition develops and consumers have adequate multichannel video programming alternatives."[17] Moreover, promotion of the emergence of effective competition through the entry of alternative distribution technologies is a critical element of the regulatory framework mandated by Congress.[18] The Commission has adopted rules implementing this mandate; in particular, regulations requiring that programming be made available to competing distributors on non-discriminatory terms, and prohibiting cable operators from discriminating against unaffiliated programmers on the terms and conditions of carriage.[19] In this manner, the Commission has sought to inhibit anticompetitive abuses and to foster the emergence of a competitive market for the delivery of video programming to consumers.

B. Scope of the *Report*

7. Through this *Report* and future reports, the Commission intends to provide Congress with information regarding the state of competition in the market for the delivery of video programming, with a particular emphasis on the cable television industry. Accordingly, this *Report* provides data and information on: cable industry performance (Section II); the status of entry by Multichannel Video Program Distributors ("MVPDs"), including those that use technologies other than cable (Section III); and structural issues

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[15] Communications Act § 623(a)(2), 47 U.S.C. § 543(a)(2).

[16] *Id.*

[17] *NOI* ¶ 2, 9 FCC Rcd at 2896.

[18] *See* 1992 Cable Act, secs. 2(b)(1-2) (articulating Congressional policy to "promote the availability to the public of a diversity of views and information through cable television and other video distribution media" and to "rely on the marketplace, to the maximum extent feasible, to achieve that availability"); Communications Act § 623(a), 47 U.S.C. § 543(a) (prohibiting rate regulation if the Commission "finds that a cable system is subject to effective competition" and defining "effective competition" with specific regard to competition to cable from other "multichannel video programming distributors").

[19] *See generally Program Access Report & Order*, 8 FCC Rcd 3359; *Implementation of Sections 12 & 19 of the 1992 Cable Act -- Dev. of Competition & Diversity in Video Programming & Carriage, Second Report & Order* ("*Program Carriage Report & Order*"), 9 FCC Rcd 2642 (1993), *recon. granted, Memorandum Opinion & Order,* FCC 94-203 (MM Docket No. 92-265 Aug. 5, 1994).

affecting entry, such as vertical integration, horizontal concentration, and technological advances (Section IV). Also included in Section IV are preliminary assessments of the impact of the 1992 Act and of the Commission's regulations on access to video programming services by competing MVPDs.

8. Section V of the *Report* contains the Commission's analysis of the extent of competition in the market for the delivery of video programming, and an assessment of market performance. A discussion of future action by the Commission to study the cable industry and to prepare for future reports is also included in Section V.

9. In preparing this *Report*, the Commission has been mindful of the rate regulation provisions of the 1992 Act, which exempt from rate regulation cable systems subject to "effective competition."[20] As described more fully below, the 1992 Cable Act defines "effective competition" to exist when: (a) a franchise area is served by at least two unaffiliated MVPDs, each of which offers comparable video programming to at least 50% of the households in the franchise area; and (b) at least 15% of the households in the franchise area subscribe to service from MVPDs other than the largest one.[21] The statute also defines effective competition to exist when fewer than 30% of the households in the franchise area subscribe to the cable system, or when an MVPD operated by the franchising authority offers service to at least 50% of the households in the franchise area.[22] The term "MVPD" is defined in the 1992 Act as "a person, such as, but not limited to, a cable operator, a multichannel multipoint distribution service ["MMDS"], a direct broadcast satellite ["DBS"] service, or a television receive-only ["TVRO"] satellite program distributor, who makes available for purchase, by subscribers or customers, multiple channels of video programming."[23]

10. As explained in Section III.A.4, *infra*, the competitive status of MVPDs is an appropriate starting point for this *Report*. However, Congress charged the Commission with annually reporting on the "status of competition in the market for the delivery of video programming."[24] In the Commission's view, obtaining a complete picture of the status of competition requires the Commission to look beyond MVPDs to other technologies not explicitly included within the statutory definition that may have a constraining effect on cable system practices.[25] Moreover, to fulfill its statutory mandate, the Commission believes it should also look beyond the "effective competition" standard of the 1992 Cable Act, which is

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[20] Communications Act § 623(a)(2), 47 U.S.C. § 543(a)(2).

[21] Communications Act § 623(l)(1), 47 U.S.C. § 543(l)(1).

[22] *Id.*

[23] Communications Act § 602(12), 47 U.S.C. § 522(12).

[24] Communications Act § 628(g), 47 U.S.C. § 548(g).

[25] *See infra* ¶¶ 46-53.

a bright-line test used to determine when a particular cable system's rates may be deregulated. Accordingly, in this *Report* and future reports, the Commission intends to provide a fuller economic analysis of the industry, rather than simply report on the status of "effective competition" in each franchise area in the country.

C. Summary of Findings

11. In this *Report*, the Commission makes the following findings:

12. Industry Growth. Between the end of 1990 and the end of 1993, cable industry subscriber penetration, average system channel capacity, the number of programming services available, cable industry revenues, expenditures on programming, and capital investment all increased. Data for the first half of 1994 that is available from companies that file reports with the Securities and Exchange Commission ("SEC"), while incomplete, suggest that subscribership and capital investment have increased for those companies from 1993 levels. In addition, ten of the fifteen largest cable system operators for which information is publicly-available, including the two largest such companies, have reported increases in cable service revenue for the first half of 1994, while the other five have reported decreased cable service revenues.

13. Cable Market Power. The market for the distribution of multichannel video programming remains heavily concentrated at the local level, and for most households, cable television is the only provider of multichannel video programming. Cable systems continue to have substantial market power at the local distribution level.

14. Horizontal Concentration. Since 1990, there has been a moderate increase in the horizontal concentration of cable multiple system operators ("MSOs") nationwide and, if consummated, several recent proposed mergers will result in increased "clustering" or regional concentration of cable system ownership.

15. Competitive Entry. There are presently only a few scattered areas of the country in which local cable systems face direct competition *via* "overbuilding" (where more than one cable system has cable lines passing the same homes). Providers using alternative video programming distribution media have not yet reached the subscribership levels necessary for the Commission to conclude that vigorous rivalry currently exists in the market for multichannel video programming distribution. However, alternative distribution media have made substantial strides since the *1990 Cable Report*. In particular:

- DBS service, merely a vision in 1990, is now operational, and is being rolled out around the country. It has been suggested that initial demand for the equipment necessary to receive DBS service has exceeded supply;

- MMDS or "wireless" cable systems are increasing in number, and are now obtaining the financial resources necessary for growth and expansion;

- Satellite Master Antenna Television ("SMATV") systems are growing in terms of numbers of systems and subscribers;

- in 1992, the Commission adopted a regulatory framework that permits companies providing local telephone service (commonly referred to as "local exchange carriers" or "LECs")[26] to construct and operate in their service territories common carrier platforms through which multiple entities can provide programming and other services to subscribers. Pursuant to that video dialtone ("VDT") framework, the Commission has authorized five technical or market trials and one permanent VDT service offering. In addition, there are twenty-three applications pending to provide permanent VDT service in other communities which, if granted, would allow service to 8.5 million homes; and

- other possible technological and regulatory advances have been identified that might allow broadcast television, low power television, Local Multipoint Distribution Service ("LMDS") and/or electric utilities to enter into the market for the distribution of multichannel video programming.

16. Vertical Integration. Vertical integration in the industry has remained at roughly the same level as in 1990, with cable MSOs continuing to invest in video programming vendors. The Commission anticipates that this investment will continue, and that the Commission's program access and program carriage rules will remain needed to guard against abuses that may result from such investment. Generally, those rules seem to have been successful in ensuring the availability of programming. Several firms that package programming for distribution to home satellite dish ("HSD") owners, however, have alleged that they continue to pay higher prices for programming than comparable cable operators.

[26] A glossary of technical terms and acronyms is included in Appendix B.

II.
CABLE INDUSTRY PERFORMANCE SINCE 1990

17. In this section of the *Report*, the Commission addresses the basic performance of firms that own or operate franchised cable systems.[27] This includes analysis of the following characteristics: (1) *output* -- the current amount of cable industry service that is being produced, and recent trends in that production; (2) *quality* -- the nature of the service, which is related to output since higher quality services are more highly valued and can, therefore, be thought of as more output; (3) *revenue* -- the income that is earned from the industry's output; (4) *expenditures and cash flow* -- the costs associated with the production of the industry's output; (5) *capital investment* -- the amount of investment by the companies in the industry; and (6) *transactions* -- the changes in ownership and trend towards consolidation in the industry. Section V of the *Report* contains a discussion of indicia of market power, including cable industry pricing, which is also an important indicator of industry performance.

A. Performance from 1990 to 1993

18. Cable Industry Output. Since the Commission last reported on the status of competition in this market in 1990,[28] the cable industry has continued to expand. The number of homes that could receive cable service ("homes passed") grew to 92.9 million in 1993 (up from 86 million in 1990), which was over 96% of all television households in the United States.[29]

19. With cable services available to more homes than ever before, the total number of households subscribing to basic cable services has increased to 57.4 million households, which is almost 60% of the television households in the United States (up from 51.7 million households and 55.8% of television households in 1990). The industry's penetration (which measures the percentage of households passed by cable that choose to subscribe to basic cable

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[27] As will be discussed in Section V.2, *infra,* industry performance, together with other factors, can be used to assess the extent of competition in the market. The *Report* contains data on the cable industry as a whole to the extent such information is available. As noted in the body of the *Report*, however, for certain information, particularly for the recent developments reported in Section II.B, data is only available for companies that make information publicly available, and should not be deemed to be necessarily representative of the entire industry.

[28] *1990 Cable Report*, 5 FCC Rcd 4962.

[29] *See* Appendix C, Table 1 (summarizing information, from, *inter alia, History of Cable & Pay TV Subscribers & Revenues*, CABLE TV INVESTOR, Mar. 31, 1994, at 9). Tables 2-10 referred to in this section are also included in Appendix C.

services) increased by 2.78% since the *1990 Cable Report*, so that nearly 62% of all households that could receive basic cable in 1993 purchased such services.[30]

20. Attributes of Cable Industry Service. The attributes or "quality" of cable services are multi-dimensional, and thus, no single measure of quality is available. Possible indices of cable service quality are the channel capacity of cable systems and the quantity of cable programming. Since 1990, average channel capacity has noticeably increased in the industry. Cable systems with the capacity for providing thirty or more channels accounted for over 77% of all cable systems for which information was available in 1993.[31] At the same time, systems that have capacities of twelve or fewer channels, which accounted for over 22% of all systems in 1987, accounted for only a little over 7% of all systems last year. As a result, by the end of 1993, nearly 97% of all subscribers for which information is available received service from systems that could provide at least thirty channels.[32]

21. Since the Commission issued the *1990 Cable Report,* there has also been noticeable growth in the number of cable programming choices. The number of basic programming networks grew by over 18%, from sixty-one at the end of 1990 to seventy-two at the end of 1993. The number of pay-per-view networks nearly doubled, from seven in 1990, to thirteen at the end of 1993. Overall, the number of programming networks increased by over 29%, from seventy-seven at the end of 1990, to ninety-nine at the end of 1993.[33]

22. Cable Industry Revenue. The cable industry continued to generate increased amounts of revenue between 1990 and 1993. It appears that the cable industry generated $22.94 billion in total revenue in 1993, which was over 28% more than the $17.86 billion it generated in 1990.[34] Of the 1993 amount, $13.55 billion, or over 59%, came from basic service tier programming.[35] Revenue from pay-per-view programming increased 102% from $253 million to $512 million over the same time period.

23. Advertising revenue has become an increasingly important source of revenue for the cable industry. Last year, cable operators' revenue from local and national spot

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[30] *Id.*

[31] *See* Appendix C, Table 2. The 77% of systems that can offer 30 or more channels represents a significant increase from the 67% figure in 1990.

[32] *See* Appendix C, Table 3.

[33] *See* Appendix C, Table 4.

[34] *See* Appendix C, Table 5.

[35] *Id.*

advertisement volume reached $1.064 billion,[36] up from $628 million in 1990.[37] Accordingly, advertising services provided cable systems with over 69% more revenue in 1993 than was the case in 1990.[38]

24. Cable Industry Expenditures and Earnings Before Interest, Taxes, Depreciation, and Amortization. Cable expenditures on programming rose by more than 25% between 1990 and 1993.[39] It appears that most of that increase came from substantial increases in expenditures for basic programming, which increased by 55% from $1.4 billion in 1990, to nearly $2.2 billion in 1993. Expenditures for other programming appear to have remained nearly constant over the same time period.[40]

25. Measurements of earnings before interest, taxes, depreciation, and amortization ("EBITDA"), which people in the industry commonly refer to as "cash flow," are often used to value the economic health of industry firms. It is difficult to generate such a measure for the cable industry as a whole because a significant percentage of subscribers are served by systems that do not publicly report financial information. Paul Kagan Associates, Inc. ("Kagan") has produced industry-wide cash flow estimates of $5 billion in 1987, $7.8 billion in 1990, and $10.1 billion last year.[41] For the purposes of this *Report*, the Commission has also produced an estimate of industry-wide cash flows for the same years.[42] Based on the

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[36] *Cable & Pay TV Subscribers & Revenues*, CABLE TV INVESTOR, Mar. 31, 1994, at 9; *see also* Kathy Healy, *Marketers Tune in to Cable's Appeal; Improvements Lead to Big Gains in Ad Spending*, ADVERTISING AGE, Feb. 28, 1994, at C-3 (reporting advertising revenues were greater than reported in CABLE TV INVESTOR).

[37] *See* Appendix C, Table 5.

[38] Expectations that cable networks will continue to draw large shares of the television audience were recently demonstrated by advertisers' upfront purchase of over $1 billion in commercial time from cable networks for the 1994-95 season, up 19% from last year's sales. Alan Breznick, *Advertising: Upfront '94 Wrapup*, CABLE WORLD, Aug. 29, 1994, at 40; Kent Gibbons, *Ratings Up, Cable '94 Ad Revenue Up 18%*, MULTICHANNEL NEWS, Sept. 12, 1994, at 16.

[39] *See* Appendix C, Table 6.

[40] *Id.*

[41] *See* PAUL KAGAN ASSOCS., INC., CABLE TV FINANCIAL DATABOOK ("1994 FINANCIAL DATABOOK") 88 (1994); PAUL KAGAN ASSOCS., INC., CABLE TV FINANCIAL DATABOOK ("1990 FINANCIAL DATABOOK") 118 (1990).

[42] The Commission arrived at its estimate of industry-wide cash flows by analyzing and extrapolating from the publicly-available information for fifteen of the largest cable industry MSOs. To the extent there are significant differences between the average financial

(continued...)

Commission's estimates, it appears that the industry generated cash flows of over $4.8 billion in 1987, $7.9 billion in 1990, and $10.5 billion in 1993.[43] It also appears that the industry had a cash flow per basic subscriber of $164.29 in 1993, which would represent an increase of 19% for the period between 1990 and 1993. Moreover, it appears that the industry's cash flow represented over 46% of its total revenue in 1993, which was a 4.4% increase over 1990.[44]

26. Capital Investment. In 1990, the industry invested nearly $3.0 billion in construction.[45] In 1991 and 1992, however, investment in construction dropped off, to approximately $2.2 billion in each of those years. The cable industry's construction investment rebounded in 1993, however, to almost the same level as in 1990, nearly $3.0 billion.[46]

27. Cable System Transactions. In 1990, systems with an aggregate value of $1.07 billion were sold, compared with the aggregate value of $11.21 billion for systems sold in 1987.[47] In 1993, however, the systems sold had an aggregate value of over eight billion dollars, even though the total number of transactions declined from 1990. The dollar value per subscriber of systems sold increased by over five percent during the same years, from $2049 in 1990, to $2160 in 1993.[48]

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[42](...continued)
performance of these large MSOs and that of smaller MSOs, those differences may affect the reliability of industry-wide estimates.

[43] *See* Appendix C, Table 7.

[44] *Id.* That 46% figure represents the industry's total cash flow divided by its total revenue, which is commonly referred to in the industry as "cash flow margin." It means that the industry had 46% of its total revenue on hand after accounting for operating expenses, but before accounting for interest, taxes, depreciation and amortization. Because the estimates for industry-wide cash flows are derived from the average cash flow margin for those larger MSOs that make such information publicly available, the degree to which the estimates are representative of the industry as a whole may be affected by any differences between the financial performance of smaller MSOs and that of larger MSOs.

[45] *See* 1994 FINANCIAL DATABOOK, *supra* note 41, at 92.

[46] *Id.*

[47] *See* Appendix C, Table 9.

[48] *Id.*

B. Recent Developments

28. In this section of the *Report*, the Commission provides data describing subscriber growth, revenue, capital investment and cable system transactions for the first half of 1994. The figures for subscriber growth, revenue and investment are taken from statements of cable system operators that publicly report such information in filings with the SEC. Those companies accounted for service to approximately fifty-five percent of all basic subscribers at the end of 1993, and they earned approximately fifty percent of all cable service revenue that year.[49] For many other MSOs, however, most of the relevant information is not publicly available, particularly in the case of privately-owned companies, which include most of the smaller MSOs.[50] Consequently, the information reported in the following discussion of recent developments is not necessarily representative of recent developments for the entire industry.

29. Subscriber Growth. The record indicates that the publicly-reporting companies have experienced continued growth in the number of basic subscribers over the first six months of 1994.[51] MSOs that have released reports this year that indicate recent subscriber growth include:

- the industry's largest MSO, TCI Communications, Inc. ("TCI"), which reported that it added 150,000 basic subscribers between the end of 1993 and March 31, 1994;[52]

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[49] *See* Appendix C, Table 7.

[50] The Commission has taken steps to lessen the impact of rate regulation on the revenues of small systems and operators. In particular, the Commission has created alternative regulatory approaches for small systems and operators that are designed to reduce the administrative burden associated with rate regulation, as well as the impact of the 17% percent rate reduction implemented in its March 30, 1994, order regarding rate regulation. *Implementation of Sections of the 1992 Cable Act: Rate Regulation, Second Order on Reconsideration, Fourth Report & Order, & Fifth Notice of Proposed Rulemaking* ("*1994 Rate Report & Order*") ¶¶ 117-135, 201-228, FCC 94-38 (MM Docket No. 92-266, Mar. 30, 1994).

[51] For discussions of possible explanations of the recent increase in subscriber growth, *see* Appendix I. *See also* John M. Higgins, *Re-Reg Credited for Helping Subs Gains*, MULTICHANNEL NEWS, Sept. 5, 1994, at 1.

[52] Tele-Communications, Inc., *TCI Reports First Quarter Results* (Press Release May 16, 1994).

- Adelphia Communications Corporation ("Adelphia"), which reported that it had 1.37 million basic subscribers at the end of the second quarter of 1994, up 8.4% from the same time in 1993;[53]

- Cablevision Systems Corporation ("Cablevision"), which recently reported that the average number of subscribers it served in each of the first two quarters of 1994 was 9% greater than the average for the corresponding quarters of 1993;[54]

- Viacom Cable ("Viacom"), which reported that it "added 6,500 incremental basic customers in the second quarter of 1994, approximately 266% over the amount added in the second quarter of 1993," and that since June 30, 1993, its subscribers have grown 3%, to 1,117,000;[55]

- E.W. Scripps Company ("E.W. Scripps"), which reported that as of the end of the second quarter of 1994, it had 715,700 basic subscribers, up 5.1% from the prior year, and that its penetration rate increased from 59.9% to 61.9% in the same period;[56]

- various cable system partnerships managed by Jones Intercable, Inc. ("Jones Intercable"), which reported basic subscriber growth in the twelve months ended June 30, 1994, most in the 5-6% range;[57]

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[53] ADELPHIA COMMUNICATIONS CORP., FORM 10-Q 6 (June 30, 1994).

[54] CABLEVISION SYSTEMS CORP., FORM 10-Q 15 (June 30, 1994).

[55] VIACOM INC., FORM 10-Q 18 (June 30, 1994).

[56] E.W. SCRIPPS CO., FORM 10-Q 25 (June 30, 1994).

[57] *See* JONES CABLE INCOME FUND IC LTD., FORM 10-Q 9 (June 30, 1994) (increase of 6%, from 57,198 to 60,894 subscribers); JONES INTERCABLE INVESTORS LP, FORM 10-Q 9 (June 30, 1994) (6% increase, from 72,689 to 76,990); CABLE TV FUND 12A LTD., FORM 10-Q 9 (June 30, 1994) (increase of 5%, from 63,715 to 67,103 subscribers); CABLE TV FUND 12B LTD., FORM 10-Q 10 (June 30, 1994) (increase of 2%, from 63,825 to 64,933 subscribers); CABLE TV FUND 12C LTD., FORM 10-Q 10 (June 30, 1994) (increase of 5%, from 208,474 to 219,403 subscribers); CABLE TV FUND 12D LTD., FORM 10-Q 9 (June 30, 1994) (increase of 5%, from 208,474 to 219,403 subscribers); CABLE TV FUND 14A LTD., FORM 10-Q 11-12 (June 30, 1994) (subscribers in wholly-owned systems up 6%, from 88,657 to 93,978; in non-wholly owned system, subscribers up 5%, from 43,082 to 54,324); CABLE TV FUND 14B LTD., FORM 10-Q 12 (June 30, 1994) (subscribers in wholly-owned systems up 5%, from 22,718 to 23,864).

- Cablevision Industries Corporation ("CVI") reported that it now serves 977,000 subscribers, and added 35,000 basic subscribers in the past year from internal growth of systems, in spite of the Los Angeles earthquake in January, which resulted in a loss of 5000 subscribers;[58]

- Century Communications Corporation ("Century"), whose recent annual report states that the number of subscribers it serves increased 2.4% from 919,000 on May 31, 1993, to 941,200 on May 31, 1994;[59] and

- Times Mirror Company ("Times Mirror"), which stated in its last quarterly report that specifically discussed its cable television operations that it experienced 3% internal basic subscriber growth between March 1993 and March 1994.[60]

30. Revenues. Information from cable system operators that make financial information publicly-available through the SEC indicates that cable systems revenues have remained relatively steady through the first six months of 1994. According to the most recent annual or quarterly reports of fifteen cable system operators, ten reported increased cable system revenues and five reported decreases.[61] For example:

- TCI reported an overall 4% revenue increase for the first half of 1994, compared to the corresponding six-month period in 1993. According to its second quarter report, the increase in revenue that resulted from an increased number of subscribers exceeded the decrease in revenue that resulted from rate regulation;[62]

- Time Warner Cable ("Time Warner") reported slightly increased revenues for the first six months of 1994, stating that, "the

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[58] CABLEVISION INDUSTRIES CORP., FORM 10-Q 11 (June 30, 1994).

[59] CENTURY COMMUNICATIONS CORP., FORM 10-K 31 (May 31, 1994).

[60] TIMES MIRROR CO., FORM 10-Q 11 (March 27, 1994).

[61] Those fifteen cable system operators are Adelphia, Cablevision, CVI, Century, Comcast, E.W. Scripps, Falcon Cable Systems Co. ("Falcon Cable"), Falcon Classic Cable Income Properties, L.P. ("Falcon Classic"), Multimedia Inc. ("Multimedia"), TCA Cable TV, Inc. ("TCA"), TCI, Time Warner Cable ("Time Warner"), Times Mirror, Viacom and The Washington Post Co.

[62] TCI COMMUNICATIONS, INC., FORM 10-Q I-21 (June 30, 1994).

unfavorable effects of rate regulation were offset in part by an increase in subscribers and unregulated revenues;"[63]

- Cablevision reported a 13% increase in its net revenues for the first six months of 1994, compared to 1993, most of which it attributed to a nine-percent internal growth in its number of basic subscribers;[64] and

- Adelphia reported that "[r]evenues increased approximately 5.5% for the three months ended June 30, 1994, compared to the same period in the prior year. Approximately 86% of such increases were attributable to basic subscriber growth, with the remainder primarily attributable to the expansion of advertising sales and other services."[65]

CVI, Century, Falcon Classic, Multimedia, TCA and Times Mirror also reported increased revenues.[66]

31. On the other hand, several MSOs reported decreases in revenues during the first six months of 1994. Comcast's service income for its cable division was down nearly $24 million in the first half of 1994, as compared to the first half of 1993.[67] E.W. Scripps reported that its revenues from basic service in the second quarter of 1994 were down 6.3%

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[63] TIME WARNER INC., FORM 10-Q 7 (June 30, 1994).

[64] CABLEVISION SYSTEMS INC., FORM 10-Q 14 (June 30, 1994).

[65] ADELPHIA COMMUNICATIONS CORP., FORM 10-Q 7 (June 30, 1994).

[66] CABLEVISION INDUSTRIES CORP., FORM 10-Q 3, 11 (June 30, 1994) (revenues in first half of 1994 up 1.9% over first half of 1993, "attributable principally to internal subscriber growth" and other sources); CENTURY COMMUNICATIONS CORP., FORM 10-K 31 (May 31, 1994) (cable television operation revenues increased 5.4% in fiscal year ended May 31, 1994, attributed to "increases in the number of cable television subscriptions and in the subscriber revenues for cable television services"); FALCON CLASSIC CABLE INCOME PROPERTIES, L.P., FORM 10-Q 4, 7 (June 30, 1994) (revenues in first half of 1994 up 6.8% over first half of 1993; 52% due to increase in the number of subscribers); MULTIMEDIA INC., FORM 10-Q 2 (June 30, 1994) (revenues up 1%); TCA CABLE TV, INC., FORM 10-Q 9 (July 31, 1994) (third quarter revenues up 7% over last year, "mostly attributable to internal growth"); TIMES MIRROR CO., FORM 10-Q 11 (May 27, 1994) (cable revenues up 8.6% over last year due to continued subscriber growth and other revenues).

[67] COMCAST CORP., FORM 10-Q 9 (June 30, 1994).

from the same period of 1993, despite a 5.1% increase in basic subscribers.[68] Viacom's cable revenues decreased 4% in the second quarter of 1994, including $6 million in revenue losses from the mandated rate decreases.[69] Falcon Cable and The Washington Post Company each reported cable revenue decreases of approximately 1%.[70]

32. Capital Investment. The cable industry also appears to be substantially increasing its capital investment in infrastructure development. Kagan projects that the industry will invest nearly $3.8 billion in construction this year, which is a twenty-eight percent increase over the amount invested in construction in 1993.[71] TCI alone has a capital budget of $1 billion for 1994 "for the continued rebuilding of its cable systems."[72]

33. In February, Multimedia announced a $150 million upgrade of its cable operations over the next five years, which will include spending $45 million in both 1994 and 1995 to replace coaxial wire with fiber.[73] Century increased its budget for capital expenditures in its cable operations by twenty-three percent over fiscal year 1993, from approximately $37.4 million to $46.1 million.[74] Century plans to "expand the operations of certain cable television systems into adjacent and previously unbuilt areas," as well as to upgrade its existing cable plant.[75] CVI's most recent quarterly report stated that the company plans to spend $68 million in 1994 for purposes such as expanding channel capacity, deploying fiber optic technology, and increasing the number of addressable converters.[76]

34. Time Warner has reported that it will spend $750 million this year on cable capital investment, more than twice its 1993 cable capital outlays of $353 million.[77] Time Warner also reported earlier this year, however, that the $750 million represented a reduction

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[68] E.W. SCRIPPS CO., FORM 10-Q F-21 (June 30, 1994). E.W. Scripps also reported that its cable operating income was down 36.6% in the same period. *Id.*

[69] VIACOM INC., FORM 10-Q 18 (June 30, 1994).

[70] FALCON CABLE SYSTEMS CO., FORM 10-Q 3-4 (June 30, 1994); THE WASHINGTON POST CO., FORM 10-Q 8 (June 30, 1994).

[71] 1994 FINANCIAL DATABOOK 88.

[72] TCI COMMUNICATIONS, INC., FORM 10-Q I-19 (June 30, 1994).

[73] MULTIMEDIA INC., FORM 10-Q 2 (June 30, 1994).

[74] CENTURY COMMUNICATIONS CORP., FORM 10-K 75 (May 31, 1994).

[75] *Id.* at 35.

[76] CABLEVISION INDUSTRIES CORP., FORM 10-Q 12 (June 30, 1994).

[77] Mark Robichaux, *Time Warner Trims Cable-TV Budget Due to Rate Cuts*, WALL ST. J., May 5, 1994, at B-7; *see also* TIME WARNER INC., FORM 10-Q 11 (June 30, 1994).

of $100 million from the amount that had been budgeted for 1994, due to rate reductions mandated by the Commission.[78] E.W. Scripps spent 40.8% less on cable capital expenditures in the second quarter of 1994, and 30.7% less in the first half of 1994, as compared to the same periods in 1993, even though it now serves 5.1% more subscribers than in 1993.[79]

35. Leading suppliers of cable hardware have reported substantial increases in sales this year. In particular, General Instrument Corp. ("GI") reports that its sales are up by over 64% for the first half of this year, and that its second quarter sales were 24% higher than its first quarter sales. Moreover, recent reports indicate GI's production of cable converter boxes has doubled from 9000 to 18,000 units per day, and GI is reported to attribute its increased sales to "increased cable television operator infrastructure spending . . . ."[80]

36. Cable System Transactions. There has been considerable activity in the market for cable system transactions during 1994.[81] The thirty-eight transactions announced in 1994 that have been identified by the Commission have a total dollar value of nearly $10.95 billion which, if the transactions are consummated, would be significantly greater than the $8.32 billion that changed hands in 1993.[82] However, the average price of $2035 per subscriber and cash flow multiple of 10.2 times cash flow are somewhat lower this year than the 1993 levels of $2160 per subscriber and 11.3 times cash flow.[83] Among the major proposed transactions that have been announced in 1994, are the following transactions involving four of the five largest MSOs:[84]

- the proposed acquisition by Comcast Cable of systems that Rogers Communications purchased from Maclean Hunter. The Rogers systems that are being purchased serve a total of 547,000 subscribers, and are being purchased for $1.27 billion;

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[78] *Id.*

[79] E.W. SCRIPPS CO., FORM 10-Q F-21 (June 30, 1994).

[80] Carl Weinschenk, *The State of GI*, CABLE WORLD, Sept. 5, 1994, at 27; GENERAL INSTRUMENT CORP., FORM 10-Q 17 (June 30, 1994).

[81] Appendix C, Table 10, lists cable system transactions announced in 1994 that have been identified by the Commission.

[82] Because dollar values for the proposed transaction between Time Warner and Newhouse Broadcasting Corp. are difficult to estimate, in large part due to the fact that a joint venture will be formed, that transaction is not included in the $10.95 billion figure for the total dollar value of transactions this year. *Time Warner to Put Some Cable Systems into Venture with Newhouse Operations*, WALL ST. J., Sept. 13, 1994, at A2.

[83] *Compare id. with* Appendix C, Table 9.

[84] *See* Appendix C, Table 10.

- the proposed acquisition by Cox Cable Communications of cable systems owned by Times Mirror serving 1.2 million subscribers, for a purchase price of $2.29 billion;

- the proposed acquisition by TCI of systems owned by Tele-Cable Corp. serving 740,000 subscribers, for a purchase price of $1.5 billion; and

- the proposed merger of certain cable systems owned by Time Warner, which serve 2.8 million subscribers, into a joint venture with cable systems owned by Newhouse Broadcasting Corp. and Advanced Publications, Inc., which serve 1.4 million subscribers. The cable systems being contributed to the proposed joint venture have been valued at $8.4 billion.

III.
STATUS OF EXISTING AND POTENTIAL COMPETITORS TO FRANCHISED CABLE SYSTEMS

A. Market Definition

37. In this section of the *Report*, the Commission first discusses the relevant market concept and how it has been applied to the cable television industry by the Commission and Congress over time. Parts B and C of this section contain discussions of various other distribution media that offer, or could offer, services that, to different degrees, may have the potential to constrain cable industry conduct.

1. The Relevant Market Concept

38. Defining the "relevant market," a concept drawn from antitrust law, is an important first step in assessing whether a firm has market power, *i.e.*, "the power to control market prices and exclude competition."[85] The relevant market has both geographic and product components, which, when defined, allow for the identification of market participants and their respective market shares.[86]

39. For the purposes of this *Report*, the Commission draws upon the relevant market concept in order to identify those distribution technologies that will potentially have a constraining effect on cable operator conduct. Therefore, as part of this and future reports, the Commission will report on the basic conditions relative to those industries, including the extent of their competition with cable operators.

40. Antitrust case law and economic theory define the relevant product market by analyzing the degree to which products or services are "reasonably interchangeable by consumers for the same purposes."[87] The geographic market is defined in a similar manner. The geographic market is the area in which products compete with substantial parity.[88] As

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[85] *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391 (1956).

[86] *See Policy & Rules Concerning Rates for Competitive Common Carrier Services & Facilities Authorizations Therefor, Fourth Report & Order* ¶ 67, 95 FCC 2d 554, 562-63 (1983) ("*Competitive Common Carrier Report & Order*").

[87] *du Pont*, 351 U.S. at 394 (1956). The use of "cross-elasticity" of demand in the process of defining a product market has received support by antitrust law commentators, economists, the Department of Justice, and courts. *See, e.g.*, William M. Landes & Richard A. Posner, *Market Power in Antitrust Cases*, 94 HARV. L. REV. 937, 945-48 (1981); George S. Stigler & Sherwin Rosen, *The Extent of the Market*, 28 J. L. & ECON. 555 (1985).

[88] *See, e.g., Satellite Television & Associated Resources, Inc. v. Continental Cablevision, Inc.*, 714 F.2d 351, 356 (4th Cir. 1983), *cert. denied*, 465 U.S. 1027 (1984).

with the definition of the relevant product market, its scope is defined by the geographic area to which buyers can reasonably turn or from which competing suppliers are likely to sell.[89]

2. *The Commission's Evolving Approach to Market Definition for Cable Services*

41. In the mid-1980s, the Commission's view of the relevant market was shaped by its implementation of the 1984 Cable Act,[90] which exempted cable systems from rate regulation unless the cable system was not subject to "effective competition" under a definition to be determined by the Commission.[91] In 1985, the Commission adopted rules that deemed "effective competition" to exist if at least three unduplicated broadcast television signals were "available" to the cable community.[92] The Commission thus concluded that three broadcast stations were sufficient to constrain monopolistic pricing of basic cable services, and defined a relevant market that included (though was not necessarily limited to) those two media.[93]

42. The Commission's view of the relevant market in which cable operators compete has evolved considerably since the *1985 Effective Competition Report & Order*. The Commission initiated a rulemaking in 1990 regarding the effective competition standard it had adopted five years earlier,[94] and later issued the *1990 Cable Report*.[95] In the *1990 Cable Report*, the Commission examined the services cable systems provided to consumers in a

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[89] *Tampa Elec. Co. v. Nashville Coal Co.* ("*Tampa Electric*"), 365 U.S. 320, 330-33 (1961).

[90] Pub. L. No. 98-549, 98 Stat. 2779 (1984).

[91] 1984 Cable Act, sec. 2, § 623(b)(1), 98 Stat. at 2788.

[92] 47 C.F.R. § 76.33(a) (1988) (superseded). Those rules were upheld in *ACLU v. FCC*, 823 F.2d 1554, 1564-70 (D.C. Cir. 1987), *cert. denied sub nom., Connecticut v. FCC*, 485 U.S. 959 (1988).

[93] The Commission based this rule on evidence that cable systems would be able to exercise market power when the share of viewership of all "cable-only" programming was as large or larger than the viewership of an over-the-air broadcast station. The Commission found that this occurred when less than three over-the-air broadcast stations were available. *Amendment of Parts 1, 63 & 76 of the Commission's Rules to Implement the Provisions of the Cable Communications Policy Act of 1984, Report & Order ("1985 Effective Competition Report & Order")* ¶ 100, 50 Fed. Reg. 18,637, 18,650 (1985).

[94] *Reexamination of the Effective Competition Standard for the Regulation of Cable Television Basic Service Rates, Notice of Proposed Rule Making,* ("*1990 Notice*"), 5 FCC Rcd 259 (1990).

[95] *1990 Cable Report*, 5 FCC Rcd 4962.

detailed manner. The Commission concluded that cable systems provide four distinct services: "antenna service" (retransmission of broadcast signals), "premium" programming (*e.g.*, HBO, Cinemax), "general interest basic channels similar to independent television stations" (*e.g.*, USA, TNT), and "specialized basic services" (*e.g.*, ESPN, CNN, MTV, BET).[96] Examining the "substitutability" of other media for each of these services, the Commission found that video cassette recorders ("VCRs") and video cassettes were good substitutes for premium services, and that local broadcast stations were good substitutes for the "antenna service."[97] The Commission then proceeded to find evidence of market power in the remaining services.[98]

43. The Commission recognized in the *1990 Cable Report* that broadcasters offer some competition to cable systems, and "can be a significant constraint on basic cable rates."[99] The Commission found, however, that "there is no close substitute for that steadily-expanding complement of specialized program services offered by the typical cable system at this time."[100] The Commission also expressly rejected defining the market as "information and leisure entertainment services" (which would include radio, print media, movie, legitimate theater and live events as alternatives).[101] As to the geographic market, the Commission concluded that the relevant market was essentially local in scope, noting that "because most cable systems operate under a local franchise, that describes the area within which they are entitled to distribute video services."[102]

44. In a concurrent rulemaking proceeding, the Commission reexamined the "three over-the-air signals" test for effective competition adopted in 1985.[103] When it sought comments in that proceeding, the Commission stated that it had replicated its prior research (which concluded that three-over-the-air broadcast signals could constrain basic cable rates),

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[96] *Id.* ¶ 50, 5 FCC Rcd at 4995.

[97] *Id.*

[98] *Id.* ¶¶ 69-70, 5 FCC Rcd at 5003.

[99] *Id.* ¶ 66, 5 FCC Rcd at 5002.

[100] *Id.* ¶ 13(2), 5 FCC Rcd at 4972.

[101] *Id.* ¶ 53, 5 FCC Rcd at 4996-97.

[102] *Id.* ¶ 48, 5 FCC Rcd at 4994.

[103] *Reexamination of the Effective Competition Standard for the Regulation of Cable Television Basic Service Rates, Report & Order & Second Further Notice of Proposed Rule Making* ("*1991 Effective Competition Report & Order*"), 6 FCC Rcd 4545 (1991).

and found that its conclusions were no longer applicable to consumer demand in 1990.[104] The Commission noted that "a small number of broadcast signals alone generally cannot deliver comparable service" to basic cable.[105] On the other hand, in the *1991 Effective Competition Report & Order*, the Commission found that if enough signals were available, broadcast television could have some constraining effect on basic cable pricing. Utilizing new econometric data, the Commission determined that six unduplicated over-the-air broadcast television stations were needed to constrain monopolistic pricing or conduct in basic services.[106]

45. In 1991, the Commission also adopted a "multichannel competitor test" that recognized competition from alternative suppliers of delivered multichannel video services by creating a "50/10" test (50% availability of alternative sources with 10% total subscribership to those alternative sources).[107] The Commission reasoned that even though alternative suppliers might offer different channel packages, "these alternatives should be considered substitutes for basic cable service since they provide a variety of programming services . . . ."[108]

3. The 1992 Cable Act

46. The 1992 Cable Act, in part, uses a conceptual view of the relevant market similar to that outlined in the *1990 Cable Report* to define the circumstances when cable rates will be exempt from rate regulation. It provides that a cable system will be subject to rate regulation unless the cable system is subject to "effective competition," a determination which is to be made through the use of a two-part test.[109]

47. First, the 1992 Cable Act identifies the types of services that are capable of constraining cable system pricing. Each such service is referred to as a "multichannel video programming distributor" ("MVPD"), and is defined as "a person . . . who makes available

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[104] *Reexamination of the Effective Competition Standard for the Regulation of Cable Television Basic Service Rates, Further Notice of Proposed Rule Making* ("*1990 Further Notice*"), 6 FCC Rcd 208 (1990).

[105] *1990 Further Notice* ¶ 5, 6 FCC Rcd at 208-09.

[106] *1991 Effective Competition Report & Order* ¶¶ 9-29, 6 FCC Rcd at 4547-51. As discussed *infra* at ¶ 191, in connection with its 1994 Rate proceeding, the Commission found evidence consistent with a finding that broadcast stations do not constrain cable rates.

[107] *Id.* ¶ 37, 6 FCC Rcd at 4552-53.

[108] *Id.*

[109] Communications Act § 623(a)(2), 47 U.S.C. § 543(a)(2).

for purchase, by subscribers or customers, multiple channels of video programming."[110] Thus, the 1992 Cable Act explicitly contemplates a relevant product market comprised of distributors that offer multichannel video programming on a subscription basis.

48. Second, the 1992 Cable Act requires determination, on a franchise-area by franchise-area basis, of when "effective competition" is deemed to exist by reference to the actual presence of MVPDs providing service in a particular locale.[111] Specifically, effective competition exists under the 1992 Act where the franchise area is served by at least two MVPDs, each of which "offers comparable video programming" to at least 50% of the households, and at least 15% of the households "subscrib[e]" to the smaller MVPD.[112] The 1992 Act provides for consideration of only those firms that have actually entered the market and are providing service in determining whether cable rates in a particular franchise area should be deregulated. The 1992 Act also contains a penetration test, whereby effective competition is deemed to exist if "fewer than 30 percent of the households in the franchise area subscribe to cable service of the cable system."[113] In addition, effective competition is

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[110] Communications Act § 602(12), 47 U.S.C. § 522(12).

[111] Before a local franchising authority ("franchisor") may regulate basic cable rates, it must be certified by the Commission under Section 623(a) of the Communications Act. 47 U.S.C. § 543(a); 47 C.F.R. § 76.906. The Commission's standards for such certification are set forth in Section 543(a)(3) of the Communications Act, 47 U.S.C. § 543(a)(3), and concern the franchisor's legal authority to regulate, the consistency of its regulations with those of the Commission, and whether its procedures are reasonable and open to all interested parties. In certification proceedings, "effective competition" is presumed not to exist in the jurisdiction in question. 47 C.F.R. § 76.906. An intervenor (typically, the local cable operator) may, however, establish that effective competition *does* exist and thus defeat rate regulation by the franchisor. 47 C.F.R. § 76.911(b).

[112] Communications Act § 623(l)(1)(B), 47 U.S.C. § 543(l)(1)(B). The Commission has adopted a two-part test for determining whether consumers are "served" by two MVPDs: each MVPD's service must both be both technically available and actually available to cable subscribers. *Implementation of Sections of the 1992 Cable Act -- Rate Regulation, Report & Order Further Notice of Proposed Rulemaking* ("*1993 Rate Report & Order*") ¶ 38, 8 FCC Rcd 5631, 5666 (1993). An MVPD's service is considered comparable if it provides at least 12 channels "including at least one channel of nonbroadcast service programming." *Id.* For purposes of determining when the 15% threshold is reached, the subscriberships of all alternative MVPDs serving at least 50% of the households in the franchise area are aggregated. *Id.* at 5662-65.

[113] Communications Act § 623(l)(1)(A), 47 U.S.C. § 543(l)(1)(A).

deemed to exist if a municipal cable system offers service to at least fifty percent of the households in the franchise area.[114]

4. Implications of Market Definition for This and Future Reports

49. Product Market. For purposes of this *Report,* the relevant product market contemplated in the 1992 Act -- multichannel video programming service -- is the appropriate starting point for assessing the status of competition in the market for the delivery of video programming. A primary focus of this *Report*, and a central concern of the 1992 Cable Act, is the extent to which MVPDs that use alternative technologies are emerging as significant competitors to cable operators. In addition to cable operators (which include direct competitors known as "overbuilders"), MMDS, DBS, and TVRO providers are specifically included within the statutory definition of an MVPD,[115] and the Commission has subsequently determined that VDT and SMATV systems should be considered MVPDs, as well.[116] Consequently, this *Report* will evaluate the status of providers utilizing each of these technologies.

50. In addition, the Commission will discuss other video programming distribution media as potential substitutes for cable services. While the use of current broadcast technology is expressly excluded from the statutory definition of an MVPD (because a broadcast station does not offer "multiple" channels of video programming and is not offered on a subscription basis), the Commission nonetheless includes a discussion of broadcast television in this *Report*, given broadcasting's potential constraining effect on cable industry conduct. Finally, the Commission discusses in this section other delivery media that arguably may have a competitive impact in the market, including low power television, programming distribution by electric utilities and VCRs.

51. Geographic Market. The proper definition of the geographic market in which cable operators compete has relevance both to the assessment of cable operators' market power, and to the administration of the "effective competition" standard of the 1992 Act, a

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[114] *Id.* at § 543(l)(1)(C), 47 U.S.C. § 543(l)(1)(C). As of September 16, 1994, a total of 135 claims raising the existence of "effective competition" in certification proceedings before the Commission have been made by cable system operators. Of these, 11 (all of which are pending), are based on the 50/15 standard of the 1992 Cable Act. The other 124 of those "effective competition" claims are based on the 30% penetration standard A total of 13 of these 124 cases have been resolved (eight have been denied, while five have been dismissed).

[115] Communications Act § 602(12), 47 U.S.C. § 522(12).

[116] *1993 Rate Report & Order* ¶¶ 21-22, 8 FCC Rcd at 5650-51. The Commission reserved judgment as to whether LMDS systems or digitally-compressed broadcast signals would fit within the statutory definition, and the Commission expressly held that leased access providers offering compressed or multiplexed multichannel video programming were not MVPDs because they used the same facilities as the cable system operator. *Id.*

topic which will be addressed in future reports. As discussed above, the scope of the geographic market is defined by the geographic area to which buyers will reasonably turn and from which competing suppliers sell their products.[117] Given the current state of competitive entry, it would seem reasonable to define, at least tentatively, the local franchise area as the geographic market relevant to an analysis of the cable industry.

52. On the other hand, it is not entirely clear that cable operators view the franchise area as the "area of effective competition."[118] While at the system level, competition may be viewed on a franchise by franchise basis, MSO operations at the firm level may be national in scope, and are often comprised of a series of regional clusters.[119]

53. Moreover, over time, it is likely that consumers will be able to purchase services from MVPDs located outside their franchise areas. For example, wireless cable and SMATV systems may serve entire metropolitan areas.[120] A LEC providing VDT service may serve an entire region of the country.[121] Finally, DBS service providers may contemplate a national market.[122] Therefore, as competitive entry increases, the definition of the geographic market for purposes of economic analysis may be broadened beyond the franchise area to account for the impact of these alternative suppliers.

B. The Status of Existing Competitors to Franchised Cable Systems

1. Overbuilders

54. The term "overbuild" describes the situation in which a second cable operator enters a local market in direct competition with an incumbent cable operator. In these markets, the second operator, or "overbuilder," lays wires in the same area as the incumbent, "overbuilding" the incumbent's plant, thereby giving consumers a choice between cable service providers.

55. In the *1990 Cable Report,* the Commission found that the number of overbuilders was "relatively small," noting reports of forty to forty-nine directly competitive

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[117] *See Tampa Electric*, 365 U.S. at 330-33; *See also* UNITED STATES DEP'T OF JUSTICE & FEDERAL TRADE COMM'N, 1992 HORIZONTAL MERGER GUIDELINES ("HORIZONTAL MERGER GUIDELINES") ¶ 1.21, 4 Trade Reg. Rep. (CCH) ¶ 13,104 at 20,573-4.

[118] *See Standard Oil,* 337 U.S. at 299 n.5; *Competitive Common Carrier Report & Order* ¶ 25, 95 FCC 2d at 563.

[119] *See infra* ¶¶ 151-55.

[120] *See infra* §§ III.B.3-4.

[121] *See, e.g.*, GTE Comments at 5-6.

[122] *See, e.g.,* DirecTV Comments at 14.

systems in operation at the time of that *Report*.[123] The Commission found, however, that "direct competition has resulted in reduced per channel rates for cable service."[124] Therefore, in order to stimulate further competition from cable overbuilders, the *1990 Cable Report* contained the recommendation that Congress: "(a) forbid local franchise authorities from unreasonably denying a franchise to potential competitors who are ready and able to provide service; (b) prohibit franchising rules whose intent or effect is to create unreasonable barriers to the entry of potential competing multichannel video providers; (c) limit local franchising requirements to appropriate governmental interests (*e.g.*, public health and safety, repair and good condition of public rights-of-way, and the posting of an appropriate construction bond); and (d) permit competitors to enter a market pursuant to an initial, time-limited suspension of any 'universal service' obligation."[125]

56. Congress incorporated the Commission's recommendations in the *1992 Cable Act* by amending § 621(a)(1) of the Communications Act to provide that:

> [a franchising authority may award . . . 1 or more franchises within its jurisdiction]; except that a franchising authority may not grant an exclusive franchise and may not unreasonably refuse to award an additional competitive franchise.[126] Any applicant whose application for a second franchise has been denied by a final decision of the franchising authority may appeal such final decision pursuant to the provisions of section 635 for failure to comply with this subsection.[127]

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[123] *1990 Cable Report* ¶ 98, 5 FCC Rcd at 5013.

[124] *Id.*

[125] *Id.* ¶ 14(1), 5 FCC Rcd at 4974.

[126] Two courts have rendered divergent interpretations of the 1992 Cable Act's exclusive franchise provisions. In *Jones Cable Partners v. City of Jamestown*, 822 F. Supp. 476, 478-79 (M.D. Tenn. 1993), the court held that an exclusive franchise remained "valid, effective and enforceable," after passage of the 1992 Cable Act on the basis that Congress had not indicated an intent to apply the 1992 Cable Act retroactively, and enjoined the City of Jamestown from creating its own competing system. In *Cox Cable Communications, Inc. v. United States*, 992 F.2d 1178, 1181 (11th Cir. 1993), however, the court refused to enjoin a cable operator from overbuilding the operations of the incumbent operator which had an exclusive franchise. The court held that the 1992 Cable Act "does not automatically invalidate existing exclusive franchises; rather it invalidates the exclusivity of such franchises when a qualified applicant requests access to the market serviced by those franchises. The 1992 Act overrules the exclusivity of government franchises by imposing a reasonableness requirement on a franchising authority's refusal to award an additional franchise."

[127] 1992 Cable Act, sec. 7(a)(1) (codified at 47 U.S.C. § 546(a)(1)). A concern has

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In addition, Congress amended the Communications Act to require a franchising authority to "allow the applicant's cable system a reasonable period of time to become capable of providing cable service to all households in the franchise area."[128]

57. In connection with its March 30, 1994 Report and Order regarding rate regulation, the Commission examined the competitive differential between markets that were overbuilt and those that were not. That competitive differential was defined as the difference in monthly average revenue per subscriber between two cable systems, otherwise identical, one of which is subject to duopolistic competition from the overbuilder, and one of which is not. The Commission's statistical analysis refined the measure of the strength of overbuild competition by taking account of the amount of overlap between competing providers. Under that analysis, the Commission determined that the rates in markets that were overbuilt were an average of sixteen percent lower than the rates in markets that were not overbuilt.[129]

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[127](...continued)
been raised that the provision of Section 621 that allows an appeal only from a *final* decision of denial by a franchising authority potentially could be used by a franchising authority to delay or preclude a potential entrant from availing itself of the remedies in the Act. The Commission would be interested in hearing of any such alleged frustration of the purpose of Section 621.

[128] 1992 Cable Act, sec. 7(b) (codified at 47 U.S.C. § 541(a)(4)(A)).

[129] *1994 Rate Report & Order* ¶ 97. Appendix C of the *1994 Rate Report & Order* contains a detailed and technical discussion of the variables and economic assumptions underlying the Commission's calculation. The Commission studied 51 overbuilds (including those by municipal providers) in connection with that order. *Id.* ¶ 96.

The National Cable Television Association ("NCTA") takes exception to the methodology used by the Commission to determine the competitive differential in overbuilt markets, and submitted in this proceeding a study prepared by Arthur D. Little, Inc., which purports to evaluate the Commission's methodology used in the *1994 Rate Report and Order*. NCTA asserts that the competitive differential found by the Commission only existed in cases of systems serving fewer than 5,000 subscribers, and that such systems are not representative of the industry. According to NCTA, when system size is taken into account, the competitive differential for overbuilt systems is reduced to almost zero. *See* NCTA Comments at 4-5, Attachment D (Arthur D. Little, Inc., Evaluation of FCC Methodology for 1994 Rate Order, Report to NCTA (June 1994)).

The Commission notes that NCTA and others have appealed the *1994 Rate Report & Order*. *See Time Warner Entertainment Co. v. FCC*, No. 93-1723 (and consolidated cases) (D.C. Cir., filed Oct. 29, 1993). Accordingly, it would be inappropriate to comment on NCTA's criticisms of the Commission's rate setting methodology in this *Report*.

58. Several economic studies of direct competition in the cable industry also show that competition from overbuilding lowers cable rates.[130] Anecdotal evidence shows positive service and rate effects from overbuilds. For example, in Glasgow, Kentucky, consumers can choose between two cable systems -- one of which is operated by the Glasgow Electric Plant Board ("GEPB"), the municipal electric utility.[131] In anticipation of overbuild entry by GEPB in June 1989,[132] the incumbent operator initially dropped its basic rate for twenty-four channel service from $23.00 to $5.95. As of September 1993, after more than four years of direct competition, the municipal operator entrant offered forty-eight channels for $13.50 a month; the incumbent charged $8.95 for thirty-seven channels.[133]

59. In a 1990 article, Thomas Hazlett reported on four instances of 1987 overbuild entry, three of which were in Florida.[134] In Orange County, an overbuilder secured a county-wide franchise permitting competition in all unincorporated areas. In response, two different incumbents each reduced their basic prices by half, from the $13.00-per-month range to the $6.50-per-month range. In Riviera Beach, the incumbent operator responded to the entry of an overbuilder in 1987 by expanding its twelve-channel basic service priced at $8.40 to a package competitive with the overbuilder's twenty-six-channel, $5.75 offering. In Dade County, Florida, the incumbent operator reduced its basic service price by one-third to match

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[130] *See* John W. Merline, *How to Get Better Cable TV at Lower Prices,* CONSUMERS' RESEARCH, May 1990, at 10-17 (duopolistically competitive cable systems have rates that average 18% lower than their monopoly counterparts, and carry an average of 21% more channels than monopoly systems); Stanford Levin & John Meisel, *Cable Television and Competition: Theory, Evidence, and Policy,* TELECOMM. POLICY (1991) (monthly rates for competitive systems are approximately $2.94 to $3.33 lower than for monopoly systems); Richard O. Beil, P. Thomas Dazzio, Robert B. Ekelund, Jr., and John D. Jackson, *Competition and the Price of Municipal Cable Services: An Empirical Study,* 6 J. REG. ECON. 410-15 (1993) (competitive market prices are, on average, $3.85 less than the rates charged in monopoly markets); George Ford, Competition in the Cable Television Industry: An Economic Analysis of Overlap Variations and Cable Prices (1994) (unpublished Ph.D dissertation, Auburn University) (monopoly prices are 21% higher than overbuild prices).

[131] Entry by electric utilities into the video distribution market, generally, is discussed in Section III.C.4, *infra.*

[132] *See* WARREN PUBLISHING, INC., 1994 TELEVISION AND CABLE FACTBOOK ("1994 FACTBOOK") at D-651; *see also* LELAND L. JOHNSON, TOWARD COMPETITION IN CABLE TELEVISION ("TOWARD COMPETITION") 20 (1994).

[133] Audrey Davidson & George Ford, *Competition Will Decrease Cable Rates,* BUSINESS FIRST, Sept. 6, 1993; Kate Maddox, *Cable Overbuilds Struggle with Retransmission,* ELECTRONIC MEDIA, June 7, 1993, at S4.

[134] Thomas W. Hazlett, *Duopolistic Competition in Cable Television,* 7 YALE J. REG. 65 (Winter 1990).

a new overbuild entrant. Finally, an overbuilder entering the market in Sacramento, California in late 1987 offered thirty-six to forty-two channels at $10.00 a month, and a $10.00 installation charge, compared with the incumbent's forty-channel, $14.50 offering. However, while the incumbent initially repriced to meet the entrant's prices, it purchased the competitor six months later.[135]

60. While most studies suggest that overbuilding produces meaningful rate effects, the extent of overbuilding seems to have remained quite limited, despite the 1992 Cable Act's explicit purpose to encourage the emergence of direct competition.[136] The Commission is aware of only a few new overbuilding proposals. One example is that of FiberVision Corporation, which has plans for several significant overbuilds in Hartford, Bridgeport, New Britain and New Haven, Connecticut.[137] In has also been reported that local authorities in Greenburgh, New York are considering allowing Northeast Networks, Inc., to overbuild and compete with the incumbent, TCI of Westchester, and have agreed to let Liberty Cable Company, Inc. provide cable service via fiber optic lines of NYNEX, the local exchange carrier. According to one report, Liberty Cable will initially provide service to two condominium complexes, and may then expand its service to additional complexes and single family homes.[138] Finally, recent press reports indicate that Cablevision, currently the nation's fifth largest MSO, is considering overbuilding several systems in New Jersey.[139] The

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[135] *Id.*

[136] The reasons for limited cable system overbuilding are undoubtedly complex, although the record in this proceeding does not provide the basis for a definitive explanation. Factors such as local franchising requirements, entry-deterring strategic behavior by the incumbent operator, and the prospective effects of possible direct competition by local telephone companies, appear to be some of the considerations that currently limit the extent of overbuilding.

[137] Incumbent Hartford operator TCI unsuccessfully brought suit to overturn the Connecticut Department of Public Utility Control's grant of a Hartford franchise to Fibervision. *See First Cable Overbuild in Conn.*, COMMUNICATIONS DAILY, Feb. 18, 1994, at 8; Geoffrey Foisie, *TCI Goes to Court to Block Overbuild*, BROADCASTING & CABLE, Apr. 25, 1994, at 38; *Overbuild Appeal Denied*, BROADCASTING & CABLE TV FAX, Sept. 13, 1994.

[138] Kent Gibbons, *C-TEC Subsidiary Wants to Overbuild TCI System*, MULTICHANNEL NEWS, July 25, 1994, at 94; John Jordan, *Liberty, TCI Battle for Cable TV Market Share in Greenburgh*, WESTCHESTER CO. BUS. J., Feb. 14, 1994 § 1, at 2; Merri Rosenberg, *Municipalities Seek Cable Improvement*, N.Y. TIMES, Jan. 9, 1994 § 13, at 13.

[139] John M. Higgins, *Dolan Vows to Overbuild N.J. Ops*, MULTICHANNEL NEWS, June 27, 1994, at 1; Mark Robichaux, *Cable Chief Casts His Eye on Competitors' Turf*, WALL ST. J., June 30, 1994, at B1; *Cablevision Systems Ponders Fiber Overbuild in Comcast Territory*, FIBER OPTIC NEWS, July 11, 1994.

Commission will track the progress of existing overbuilds and monitor the emergence of new overbuild construction on an on-going basis.

2. *Direct-To-Home Satellite Services*

61. Two distinct types of direct-to-home ("DTH") satellite services now offer video programming for subscription that is comparable to the satellite-delivered programming provided by cable television services. DBS is one. Technically, DBS service refers to satellites that transmit signals "intended for reception by the general public" operating pursuant to Part 100 of the Commission's Rules in a portion of the Ku-band.[140] At present, the only operational DBS service, as that term is defined in the Commission's rules, is the high-power Ku-band DBS service offered by Hughes Communications Galaxy, Inc./DirecTV ("DirecTV") and United States Satellite Broadcasting ("USSB"). Another service, the medium-power Ku-band service offered by Primestar Partners, L.P. ("Primestar"), is commonly referred to as "medium power DBS," although the service operates in the Fixed Satellite Service ("FSS").[141] The second type of DTH service is offered by the home satellite dish (HSD) industry, and involves the home reception of signals transmitted by satellites operating generally in the C-band.

a. Direct Broadcast Satellite (DBS)

62. In 1982, the Commission authorized DBS service,[142] and granted the first of several construction permits.[143] Even though DBS service was not yet operational at the

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[140] 47 C.F.R. § 100.3.

[141] Ku-band satellites operating in the FSS are authorized pursuant to Part 25 of the Commission's rules, 47 C.F.R. § 25, *et. seq.*, and operate in different portions of the Ku-band than DBS satellites. Though Primestar uses a satellite operating in the FSS, for ease of analysis, the service will be discussed in the DBS section of the *Report*.

[142] *Inquiry into the Development of Regulatory Policy in Regard to Direct Broadcast Satellites, Report & Order*, 90 FCC 2d 676 (1982).

[143] The United States was allotted eight orbital positions for DBS under international treaties and agreements. Each orbital position has 32 channels, and thus, there are 256 DBS channels that can be used to provide service to the continental United States ("full-CONUS service"). In 1989, the Commission decided to assign orbital positions in east-west pairs, so as to maximize the number of channels of DBS service that will be provided to the entire United States. Each assigned channel covers a specified frequency range of 24 MHz, so that, for example, channel number one at each orbital position occupies the range from 12,212 MHz to 12,236 MHz.

time, the Commission found in the *1990 Cable Report* that the medium had the potential to "readily compete with cable," provided that adequate programming was available.[144]

63. Since 1990, DBS has advanced as a potential long-term viable competitor to cable. In December, 1993, the first high-power DBS satellite ("DBS-1"), owned by DirecTV and operated jointly with USSB, was launched. DirecTV owns eleven transponders on DBS-1, and USSB owns the other five.[145] On June 17, 1994, DirecTV and USSB began providing high-power DBS service via DBS-1, and DirecTV currently is transmitting over fifty channels of subscription and pay-per-view programming.[146] On August 3, 1994, DBS-2, also owned by DirecTV, was launched; DirecTV owns all sixteen of the transponders on DBS-2.[147] When DBS-2 becomes operational, which is projected to occur on September 19, 1994, DirecTV's digital broadcast facility will purportedly be able to process and transmit as many as 216 video and audio channels simultaneously.[148]

64. DirecTV states that it will be able to increase channel capacity by increasing power and introducing a new signal compression standard, which will allow it to provide an additional fifteen to twenty channels by 1995.[149] DirecTV has also filed an application to operate a third satellite, which is scheduled to be launched in early 1995.[150] USSB, with five transponders, currently offers twenty channels, and stated in comments in this docket that improvements in encoder equipment and software will make it possible to expand its service to offer twenty-five to twenty-eight channels over the next few months.[151]

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[144] *1990 Cable Report* ¶ 104, 5 FCC Rcd at 5018.

[145] A transponder receives the signal from a transmitting earth station on one frequency and retransmits the signal on another frequency for distribution to one or more receiving earth stations.

[146] DirecTV Comments at 1-2.

[147] DirecTV, Inc., *DirecTV Successfully Launches Second Direct Broadcast Satellite,* (News Release, Aug. 3, 1994); *Demand for DirecTV/USSB Systems Exceeds Supply in First Month*, COMM. DAILY, July 19, 1994, at 2-3.

[148] Chris McConnell, *DirecTV's All-Digital Domain*, BROADCASTING & CABLE, Mar. 28, 1994, at 52. *See also*, Christopher Stern, *DirecTV Aims for Cable Viewers*, BROADCASTING & CABLE, Dec. 6, 1993, at 42.

[149] DirecTV Comments at 14-15.

[150] DirecTV Comments at 15. DirecTV reportedly intends to use this third satellite to increase pay-per-view service. *See* Mary Hillebrand, *DBS Services Look Ahead*, SATELLITE BUS. NEWS, July 13, 1994, at 1, 25.

[151] USSB Comments at 5.

65. As of September 9, 1994, DBS equipment was available in twenty-three states, and approximately 40,000 households were receiving programming via DBS.[152] DirecTV expects that DBS equipment will be available throughout the continental United States by early November 1994.[153] Subscribers receive video programming directly from the satellite through small reception dishes that are approximately eighteen inches in diameter. The home receiving equipment that is required to receive the service costs $699, and subscribers can either pay $150-200 for professional installation or purchase the installation equipment for $69.95.[154] The $699 Digital Satellite System ("DSS") unit allows a subscribing household to watch one channel at a time. In order to view two different channels on different television sets, a person must purchase an $899 DSS unit and then also purchase a $649 decoder for the second television set.[155] Thomson Consumer Electronics ("Thomson"), under the brand name RCA, produces the DSS equipment which includes the receiving dish, digital receiver and remote control. Thomson/RCA has an exclusive contract to produce DSS units for the first eighteen months or one million units, whichever occurs first.[156] After that, Sony and Thomson will both produce the DSS equipment for the next six months.[157] Thereafter, other manufacturers may be licensed to produce DSS equipment.

66. DirecTV states that despite the relatively significant initial cost, 400,000 to 500,000 DSS units will be shipped by Thomson/RCA this year, and that equipment costs will decline over time.[158] Retailers in the first five markets in which DBS service has been introduced have reported that the demand for the dishes has exceeded the supply.[159] By the end of 1994, according to USSB, approximately 10,000 locations nationwide will be carrying

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[152] Letter dated September 13, 1994 from Marvin Rosenberg, Esq., counsel for USSB, Inc., to William F. Caton, Acting Secretary, Federal Communications Commission, filed in this proceeding on September 13, 1994.

[153] Letter dated September 12, 1994 from Gary M. Epstein, Esq., counsel for DirecTV, to William F. Caton, Acting Secretary, Federal Communications Commission, filed in this proceeding on September 12, 1994 ("DirecTV Letter").

[154] DirecTV Comments at 17; USSB Comments at 10; Mary Hillebrand, *DBS Hits Thomson's Backyard*, SATELLITE BUS. NEWS, July 27, 1994, at 1, 25.

[155] *Thomson, DBS Shine at CES*, SATELLITE BUS. NEWS, June 16, 1993, at 1, 21; Comments of USSB at 9.

[156] *See* DirecTV Letter.

[157] *Id.*

[158] DirecTV Comments at 16-17. *See also* USSB Comments at 8.

[159] USSB Comments at 7; *Demand for DirecTV/USSB Systems*, *supra* note 147, at 2. Those five markets are Albuquerque, New Mexico; Jackson, Mississippi; Little Rock, Arkansas; Shreveport, Louisiana; and Tulsa, Oklahoma.

DSS equipment and offering both USSB and DirecTV programming.[160] As part of its marketing effort, Hughes has also entered into an agreement with the National Rural Telecommunications Cooperative ("NRTC") to provide DirecTV services to subscribers through its membership across the country.[161]

67. In addition to DirecTV and USSB, several other ventures are attempting to enter the high-power DBS field. EchoStar Communications Corporation ("EchoStar"), which has reportedly raised $332 million dollars in a debt offering, is required by the terms of its construction permit to have its system in operation by August 15, 1995.[162] Directsat Corporation and Direct Broadcast Satellite Corporation, which are each authorized to provide eleven channels of service,[163] are required by their construction permits to be operational by August 15, 1995.[164] Tempo Satellite, Inc. (a wholly-owned subsidiary of TCI), is authorized to provide eleven channels of service and is required to be operational by May 1, 1998.[165] The other parties, which have received conditional construction permits, but have not yet been assigned specific orbital positions and channels, are Continental Satellite Corporation, and Dominion Video Satellite, Inc. According to the terms of its construction permit, Continental's DBS system is to be operational by December 4, 1996.[166] Finally, Advanced Communications Corporation, which has been assigned orbital positions and channels, is required to have its system operational by December, 1994.[167]

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[160] USSB Comments at 6.

[161] NRTC Comments at 5.

[162] *Eying Charlie Ergen's World*, SATELLITE BUS. NEWS, May 18, 1994, at 6. *Cf.* Dinah Zeiger, *EchoStar Moves into Satellite-TV Spotlight*, DENVER POST, Mar. 29, 1994, at C1 (EchoStar filed with the SEC documents describing a $335 million debt offering).

[163] EchoStar and SSE Telecom Inc. have filed an application seeking Commission consent for transfer of control of Directsat from SSE to EchoStar which would combine the allocation of channels of both EchoStar and Directsat. *See* FCC File No. DBS-88-01\88-02\94-08 TCP\M.

[164] *Application of Continental Satellite Corp. for Assignment of DBS Channels, Memorandum Opinion & Order*, 4 FCC Rcd 6292 (1989) (applying 47 C.F.R. § 100.19).

[165] *Application of Tempo Satellite, Inc. for Assignment of DBS Channels, Memorandum Opinion & Order*, 7 FCC Rcd 2728 (1992) (applying 47 C.F.R. § 100.19).

[166] *Id.*

[167] *Application of Advanced Communications Corp. for Assignment of DBS Channels, Memorandum Opinion & Order*, 6 FCC Rcd 2269 (1992) (applying 47 C.F.R. § 100.19). Advanced Communications Corporation's application for an extension of time to construct its system is currently pending before the Commission. *See* FCC File No. DBS-84-01\94-11 EXT.

68. In addition to the high-power DBS services listed above, Primestar is a joint venture owned by six MSOs, and GE American Communications, Inc., which owns the satellite used by Primestar.[168] Primestar has been operational as a medium-power Ku-band service provider since 1991,[169] and its service is available to consumers using thirty-six-inch and forty-inch dishes.[170] As of June 4, 1994, Primestar served 70,383 subscribers, and it began to use digital technology to provide service to its subscribers by digital technology on July 31, 1994.[171] Primestar is currently conducting a $55 million advertising campaign, and now offers seventy-one video channels.[172] Ultimately, after it makes a planned transition to a new generation of satellites in 1996, Primestar plans to offer more than 150 channels of programming.[173]

69. By its very nature, DBS is a national video programming distribution service.[174] DirecTV considers its potential subscriber base to be all 94 million television households.[175] However, DBS service does not offer local broadcast signals, a fact which some commenters argue inhibits the ability of DBS service to become an effective competitor

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[168] The cable companies are Comcast, Continental Cablevision, Cox Enterprises, Newhouse Broadcasting Corporation, TCI and Time Warner. *United States v. Primestar Partners*, 1994-1 Trade Cas. (CCH) ¶ 70,562 (S.D.N.Y. 1994); *State of New York ex rel. Abrams v. Primestar Partners*, 1993-2 Trade Cas. (CCH) ¶¶ 70,403, 404 (S.D.N.Y. 1993) (collectively the "*Primestar Consent Decrees* ").

[169] *Implementation of Section 25 of the Cable Television Consumer Protection and Competition Act of 1992, Direct Broadcast Satellite Public Service Obligations, Notice of Proposed Rule Making* ¶ 11, 8 FCC Rcd 1589, 1591 (1993) ("*DBS NPRM*").

[170] *DBS Duelers Cross Swords in New York*, BROADCASTING & CABLE, Mar. 21, 1994, at 40; *Arietta, New York to Be the Nation's First Digital Town*, PR NEWSWIRE, Sept. 8, 1994 (available in LEXIS, Nexis Library).

[171] Primestar Comments at 4. It was reported on September 16, 1994 that Primestar was serving more than 100,000 subscribers in forty-eight states. *Satellite and International*, COMM. DAILY, Sept. 16, 1994, at 5.

[172] *See* Primestar Comments at 4.

[173] *Id.*

[174] USSB Emergency Motion at 3.

[175] DirecTV Comments at 14 ("Since DirecTV's reach is essentially ubiquitous, all United States households are potential DirecTV subscribers"). However, DirecTV points out that local zoning ordinances or similar household access restrictions regarding residential purchase and placement of the dishes can limit DirecTV's eventual reach. *Id.* at n.21.

to cable service.[176] On the other hand, DBS service might provide consumers with service attributes that are not generally available on cable systems at this time. For example, USSB states that DBS subscribers will have digital video and compact disc ("CD") quality sound,[177] and DirecTV states that its DBS system, which has a modem in the DSS receiver, will have interactive capabilities via telephone lines.[178]

70. DBS service providers and equipment manufacturers are highly optimistic about the potential for subscribership growth. USSB predicts that between one and two million dishes will be sold within a year, and five to ten million will be sold within three years.[179] DirecTV projects that it will have over three million subscribing households within three years.[180] USSB estimates that in seven years, almost forty percent of all television households may receive programming via DSS equipment.[181] Thomson Consumer Electronics/RCA, the current manufacturer of the DBS dishes, anticipates sales of ten million units in the next six years.[182] Finally, although Primestar has concentrated its early efforts on areas unserved by cable or wireless cable,[183] it projects that it will serve in excess of 200,000 subscribers by the end of 1994, and two-to-five million by the end of the decade.[184]

b. Home Satellite Dishes (HSDs)

71. HSD technology was first developed in 1976, and commercialized in 1980.[185] HSDs are approximately 7-10 feet in diameter and receive video programming transmitted in the C-band of frequencies.[186] HSD owners can watch without payment approximately 150 unscrambled signals, and another 103 scrambled channels can be ordered through program

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[176] *See* Primestar Comments at 8; Bell Atlantic Reply Comments at 2-3.

[177] USSB Comments at 11.

[178] DirecTV Letter at 2.

[179] USSB Comments at 8.

[180] DirecTV Comments at 16.

[181] USSB Comments at 8.

[182] USSB Comments at 13.

[183] Primestar Comments at 4-5, 8.

[184] Primestar Comments at 4-5.

[185] Satellite Broadcasting and Communications Association of America ("SBCA") Comments at 3.

[186] Because signals in this band are transmitted at lower power than signals in other bands used for direct-to-home service, the receiving antenna must be larger to receive the signal.

packagers.[187] Generally, HSD owners have access to the same programming services that are available on cable, although the most popular cable programming services are scrambled.[188] In order to receive one or more scrambled channels, an HSD owner must purchase an integrated receiver-decoder ("IRD") from an equipment dealer and then pay a monthly or annual subscription fee to one of the thirty or so national packagers of HSD programming.[189]

72. In the *1990 Cable Report*, the Commission observed that HSD use in the United States had grown to roughly 2.8 million units from approximately 900,000 in 1984, and that this growth stalled in 1986 with the advent of satellite signal scrambling.[190] In addition, the *Report* noted that zoning regulations could restrict many viewers' ability to install an HSD system.[191]

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[187] SBCA Comments at 3.

[188] TOWARD COMPETITION, *supra* note 132, at 115.

[189] SBCA Comments at 8. A number of programmers and cable operators have established HSD packager units or subsidiaries. In addition, a number of unaffiliated third-parties serve as program packagers.

[190] *1990 Cable Report* at ¶ 103, 5 FCC Rcd at 5016. As noted in the *1990 Cable Report*, the market for HSD service changed significantly in 1986, when HBO first began scrambling its satellite signal and then selling it to HSD owners who had purchased a decoder. Other program services followed HBO's example and began scrambling their satellite signals. The introduction of signal scrambling in 1986 resulted in the advent of significant pirating of scrambled signals through the illegal use of decoding systems. Indeed, the first decoder used by the HSD industry, the VideoCipher II, manufactured by General Instrument, Inc., was itself susceptible to signal pirating. According to one report, by 1990 more than 50% of the users of this decoder were not paying for programming. TOWARD COMPETITION, *supra* note 132, at 116 (citing Karen J.P. Hawes, *Encryption in the '90s*, VIA SATELLITE, June 1990, at 29). According to another estimate, of the approximately 3.5 million reception systems in the United States in 1991, close to 1.2 million consumers had modified their systems so as to be able to receive scrambled programming without having to pay a fee. SBCA Comments at 7. As a result of this pirating, a second decoder was developed, the VideoCipher II Plus, which offered greater security and replaced the earlier units. TOWARD COMPETITION, *supra* note 132, at 116. SBCA indicates that VideoCipher II Plus "has held for three years now, and many of the consumers who previously owned 'chipped' units have now converted to being legitimate subscribers." SBCA Comments at 7.

[191] *Id.*

73. Today, there are approximately four million HSD users, roughly half of whom, according to SBCA estimates, subscribe to one or more programming services.[192] It has also been reported that almost all recent buyers of HSD systems are choosing to subscribe to a programming service.[193] Consumers pay an average of $2,500 for a complete HSD system,[194] although one commenter states that a C-band system can be purchased and installed for as little as $1,000.[195] There are indications that HSD use might be increasing -- SBCA reports that 55,000 C-band systems were shipped in April 1994 and another 61,000 were shipped in May 1994.[196] Those are the two highest monthly totals of C-band shipments since 1986, the year programmers began scrambling their signals.[197]

74. A survey by the SBCA indicates that HSDs and cable systems may be either complementary video programming services or substitutes for each other, depending on viewer preferences and other circumstances. That survey found that 61% of HSD systems were purchased by persons who did not have access to cable at the time they purchased the HSD.[198] However, the survey also found that 37% of HSD owners with access to cable subscribe to cable services, and that 18% of HSD owners who subscribe to satellite-programming packages also subscribe to cable.[199] Among HSD owners who subscribe to both cable and one or more satellite-programming packages, 41% did so for the purpose of receiving local television stations.[200]

75. The HSD industry's primary competitive strength *vis-a-vis* cable is programming variety and flexibility. An HSD owner may choose from a variety of program packages offered by the approximately thirty program packagers nationwide.[201] Those program packagers compete with each other to offer owners the most desirable combinations

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[192] SBCA Comments at 12; *Satellite System Sales*, SATELLITE BUS. NEWS, Aug. 10, 1994 at 1 (citing General Instrument Corp. statement).

[193] *Why Do People Buy?* SKYREPORT (Newsletter of SBCA), First quarter 1994, at 10, 11.

[194] SBCA Comments at 5.

[195] Consumer Satellite Systems, Inc., Programmers Clearing House, Inc., and Satellite Receivers, Inc. (hereinafter collectively referred to as "CSS") Comments at 2.

[196] SBCA Comments at 4.

[197] *Id.*

[198] SBCA Comments, Appendix B, at 7.

[199] *Id.*

[200] *Id.*

[201] *Id.* at 8.

of programming services at attractive prices.[202] One commenter states that the average HSD subscriber purchases programming from 2.5 different outlets.[203] The survey commissioned by the SBCA found that the most common reason for purchasing an HSD was to gain access to an increased variety of programming.[204]

76. Although HSD services offer more programming options than any other video delivery system, the cost of a system entails a large upfront expenditure by the consumer. Another drawback for HSD services comes from the fact that many localities have enacted zoning ordinances that restrict the deployment of HSDs.[205] Although the Commission has preempted zoning ordinances that either discriminate against HSDs without "a reasonable and clearly defined health, safety or aesthetic objective," or impose "unreasonable limitations" on the use of satellite dishes,[206] the SBCA reports that local authorities continue to enact ordinances that violate these rules.[207] It also notes that the Commission's ability to enforce its zoning preemption rules recently has been limited by a federal court decision.[208] Therefore, the SBCA requests that the Commission clarify its rules preempting zoning ordinances that unreasonably differentiate between satellite dishes and other types of antennas.[209] Related to the zoning problem is the SBCA's contention that homeowners' associations, through covenants and other restrictions, prohibit homeowners from deploying HSDs.[210] Although the SBCA estimates that eighty percent of all new homes in the United States are part of homeowners' associations, there is no indication of how widespread this practice may be.[211]

77. A third factor that may affect the ability of HSD systems to compete with cable systems is presented by claims that HSD program packagers are charged prices for video

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[202] Netlink Reply Comments at 3.

[203] CSS Comments at 5.

[204] SBCA Comments, Appendix B at 3.

[205] *Id.* at 17-18.

[206] 47 C.F.R. § 25.104.

[207] SBCA Comments at 18.

[208] *Town of Deerfield v. FCC*, 992 F.2d 420 (2d Cir. 1993) (where Commission rules contemplated court review of municipal zoning ordinances under limited Commission preemption, Commission may not subsequently review finding made by district court).

[209] SBCA Comments at 18. SBCA and Hughes Network Systems, Inc. have each filed a petition for declaratory ruling concerning the Commission's preemption of local zoning regulation of satellite antennas.

[210] SBCA Comments at 19.

[211] *Id.*

programming that cannot be justified under the Commission's program access rules.[212] Those claims are addressed in the Commission's discussion of the program access rules in Section IV.B.2.a of the *Report*.

3. Terrestrial "Wireless" Cable -- Multichannel Multipoint Distribution Service (MMDS)

78. The term "wireless cable" refers to the Multipoint Distribution Service ("MDS") and MMDS (Multichannel Multipoint Distribution Service), both of which transmit video programming using over-the-air microwave radio channels.[213] Subscribers use rooftop antennas to receive the programming transmitted from the wireless cable tower. The signals received are then sent through electronics equipment to the subscriber's television set. There are eleven MMDS channels available to wireless cable system operators for full-time use, and either two or three single-channel MDS channels depending on the particular city. In addition, wireless cable system operators have access to the twenty channels allocated to Instructional Television Fixed Service ("ITFS")[214] on a leased, part-time basis. Thus, wireless cable operators have access to a maximum of thirty-two or thirty-three channels.

79. The wireless cable industry has increased its subscribership from 50 systems serving 300,000 subscribers in 1990, to 143 systems serving 550,000 subscribers by June 1994.[215] In addition, analysts have projected the number of wireless cable subscribers to grow through the end of the decade.[216] Although wireless cable has not achieved significant penetration nationwide, there are a number of markets in which wireless cable has gained a foothold in competition with wired cable systems. In Riverside, California for example, Cross Country Wireless Cable TV has attracted 42,000 subscribers out of a total of 400,000 homes that can receive its services.[217] People's Choice TV in Tucson, Arizona had 22,000 subscribers as of June 1994, and projects that it will add another 18,000 subscribers over the next two years.[218] CableMaxx currently has 14,000 subscribers in Austin, Texas and is

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[212] *See, e.g.*, CSS Comments at 3-5; NRTC Comments at 9-20.

[213] Local Multipoint Distribution Service ("LMDS") also transmits multichannel video using microwave frequencies. *See infra* LMDS discussion in section III.C.2.

[214] ITFS channels are used by educational institutions to interconnect scattered campus locations.

[215] Wireless Cable Association International, Inc. ("WCA") Comments at 2.

[216] *Critical Mass for Critical Funding*, WIRELESS CABLE INVESTOR, June 30, 1994, at 1-2.

[217] *Gerard Klauer Mattison Conference*, WIRELESS CABLE INVESTOR, Mar. 30, 1994, at 5.

[218] People's Choice Comments at 7.

adding subscribers at the rate of 1000 per month.[219] ACS Enterprises, which operates in the Philadelphia, Pennsylvania area, has approximately 30,000 subscribers.[220] Finally, after just over two years of operation, Coastal Wireless Cable Television provides service to 10.5% of the homes in Ft. Pierce, Florida that are capable of receiving its signal.[221]

80. Wireless cable operators recently have gained access to financing from public debt and equity markets. Since December 1992, wireless operators have raised almost $600 million from the public markets.[222] Those funds permit wireless operators to acquire multiple systems, and thereby to begin laying the foundation for the economies of scale now enjoyed by MSOs.[223] Access to public financing also permits wireless operators to expand their systems more rapidly.[224] For example, after People's Choice TV issued stock to the public on July 8, 1993, it increased its subscriber base in Tucson, Arizona from 13,000 to 22,000, and now expects to add a total of 125,000 subscribers to its five systems by March, 1995.[225] Accordingly, it appears that access to public financing, as well as increasing credibility with banks,[226] may have helped to alleviate one of the major problems that has confronted the wireless industry.

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[219] *Gerard Klauer Mattison Conference*, *supra* note 217, at 4.

[220] Charles Reidstetter, *Trendsetter Grows A Business*, PRIVATE CABLE & WIRELESS CABLE, June 1994, at 7; John M. Higgins, *Wireless Operators Receive Money, but Find It Scarce; Wireless Cable Operators Financing*, MULTICHANNEL NEWS, Jan. 25, 1993, at 3.

[221] As of August 18, 1994, Coastal had 12,966 customers out of 129,000 households that could receive its services ("homes seen"). A recent article indicates that Coastal's subscribership may exceed 15% percent in one of the cable franchise areas where it provides wireless cable service. Tom Kerver, *Attack of the Wireless Entrepreneurs,* CABLEVISION, July 25, 1994, at 30.

[222] *Critical Mass*, *supra* note 216, at 1.

[223] For example, the door-to-door marketing now employed by many wireless cable operators will eventually give way to large scale mass media advertising. Also, wireless cable operators will qualify for bulk discount programming rates when they reach a certain level of subscribership. MARY L. KUKOWSKI, THE WIRELESS CABLE INDUSTRY -- PHOENIX RISING 8, Aug. 22, 1994 (Dillon Read Equity Research Aug. 22, 1994); *See also* Paul Read, *Skyline Goes After Cable Subscribers,* JOURNAL OF BUSINESS - SPOKANE, June 10, 1993 (wireless cable operator who relied on door-to-door marketing began advertising via television and radio).

[224] *See, e.g.*, WCA Comments at 3-4; Annette K. Hugh, *NCTA Invites Competitors To Enter Lion's Den*, PRIVATE CABLE PLUS WIRELESS CABLE, July 1994, at 17.

[225] People's Choice Comments at 7.

[226] *Gerard Klauer Mattison Conference*, *supra* note 217, at 1.

81. The wireless cable industry has a number of strengths *vis-a-vis* cable. First, wireless cable system operators appear to incur lower costs for the initial construction of their systems.[227] One analyst estimates that wireless cable systems have capital costs that are one-third lower than the capital costs of cable systems.[228] The lower initial construction cost allows wireless operators to provide comparable service at lower prices than cable.[229] Indeed, it has been argued that those lower prices are the basis for the growth of wireless cable up to this point.[230]

82. Second, it appears wireless operators may be able to upgrade their systems to employ digital compression and interactive applications at a lower cost per subscriber than cable system operators.[231] A study undertaken by People's Choice TV estimated that upgrading to digital compression and interactive applications would cost cable operators almost twice as much as wireless operators.[232]

83. Third, in contrast to cable system operators, wireless cable operators are not required to obtain franchises in order to provide service.[233] However, at least one state now

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[227] TOWARD COMPETITION, *supra* note 132, at 128. Johnson believes this is particularly true in cases where the owner of the cable system paid significantly more than the replacement cost of the system.

[228] R.S. Salomon, Jr., *Can Wireless Compete?* FORBES, Oct. 11, 1993, at 182. Another observer estimates that the total per-subscriber investment for wireless operators is $400-$500 compared with $700 per subscriber for cable. TOWARD COMPETITION, *supra* note 132, at 128.

[229] WCA Comments at 10-12. It has been reported that wireless cable rates are 25% lower than cable rates for comparable service. G. ROBERT BERZINS, WIRELESS CABLE: A STRONG COMPETITIVE THREAT TO CABLE 3 (Kidder, Peabody & Co. Research, July 20, 1994). In addition, the president of Cross Country Wireless Cable TV, Inc. recently stated that 77% of the subscribers in its Riverside, California system subscribe to Cross Country because of its lower prices. *Attack of the Wireless Entrepreneurs*, *supra* note 221, at 29.

[230] *Attack of the Wireless Entrepreneurs*, *supra* note 221, at 29. *See also* TOWARD COMPETITION, *supra* note 132, at 129 (stating that wireless cable systems' success depends on their ability to undercut their competitors' prices while offering comparable programming).

[231] *Gerard Klauer Mattison Conference*, *supra* note 217, at 1-3; BERZINS, *supra* note 229, at 3.

[232] *Gerard Klauer Mattison Conference*, *supra* note 217, at 1-3.

[233] *See Definition of a Cable Television System, Report & Order* ("*Definition of a Cable System Report & Order*"), 5 FCC Rcd 7638 (1990); *see also* TOWARD COMPETITION, *supra* note 132, at 157: ("Franchising requirements and public service obligations imposed by local governments are a major impediment to full and fair competition . . . .")

regulates various aspects of the customer service provided by wireless cable operators and other MVPDs.[234]

84. Finally, wireless systems may have technological advantages. Because radio frequencies rather than wires are used to deliver signals to subscribers, it has been suggested that there is both less signal degradation, which results in higher picture quality, and fewer outages than with cable systems.[235]

85. However, WCA has pointed to several remaining obstacles which it claims could hamper the growth of wireless cable. First, wireless cable operators have difficulty in gaining access to a sufficient number of channels to provide a competitive service.[236] As previously noted, wireless cable operators may assemble a maximum of thirty-three channels to transmit programming in any one market. Moreover, while some operators have accumulated thirty or more channels, others have encountered difficulty in obtaining licenses. That difficulty results in part from the opportunities for "warehousing" of licenses that both the MMDS and ITFS licensing methods have presented.[237]

86. In order to bring the application process under control, and to prevent further speculative filings, the Commission instituted application freezes both for new MDS

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[234] 5 Cal. Gov. Code 1(a) §§ 53088.1-53088.2.

[235] NORDBERG CAPITAL, INC., THIRD GENERATION TELEVISION 4 (Industry Study Oct. 21, 1993) Wireless cable's possible advantage in the area of signal quality may disappear as cable operators begin transmitting their signals digitally. BERZINS, *supra* note 229, at 4.

[236] WCA Comments at 6-7.

[237] *See Amendment of Part 74 of the Commission's Rules With Regard to the Instructional Television Fixed Service, Order & Further Notice of Proposed Rulemaking*, 9 FCC Rcd 3348 (1994) (addressing ITFS filing abuses and application processing issues); *Amendment of Parts 1, 2, & 21 of the Commission's Rules Governing Use of Frequencies in the 2.1 & 2.5 GHz Bands, Notice of Proposed Rulemaking*, 7 FCC Rcd 3266 (1992) (noting the volume of MMDS applications received by the Commission and instituting a freeze on these applications).

Pursuant to the Omnibus Budget Reconciliation Act of 1993, the Commission now has authority to issue certain licenses by competitive bidding. Communications Act § 309(j)(1), 47 U.S.C. § 309(j)(1). The Commission has determined that mutually exclusive applications for MDS and MMDS licenses filed after July 26, 1993 shall be resolved by using competitive bidding. *Implementation of Section 309(j) of the Communications Act - Competitive Bidding, Second Report & Order* ¶ 62, 9 FCC Rcd 2348, 2353 (1994).

stations,[238] and for new ITFS stations or major modifications to ITFS applications or facilities.[239] WCA states that these application freezes, along with extensive use of ITFS channels by educational institutions in certain markets, have slowed the accumulation of channels by wireless operators.[240] On June 9, 1994, the Commission undertook several steps aimed at eliminating regulatory delays for wireless cable licensing, one of which was to lift the application freeze for major modifications to ITFS licenses.[241] The WCA believes that the Commission's substantive and administrative improvements in wireless cable licensing will improve the Commission's ability to process the pending legal and application backlogs.[242]

87. Second, wireless cable transmitters must have line-of-sight access to a home in order for that home to be capable of receiving wireless cable service. Consequently, many homes are unable to receive service from this technology because they are blocked by trees or buildings. It has been estimated by one analyst that the average wireless cable operator has line-of-sight access to seventy-five percent of the homes in its service area.[243] That percentage varies depending on the strength of the wireless cable transmitter and the topography of the service area. WCA reports that a low-cost signal booster, which allows

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[238] *Amendment of Parts 1, 2, and 21 of the Commission's Rules Governing Use of Frequencies in the 2.1 and 2.5 GHz Bands, Notice of Proposed Rulemaking*, 7 FCC Rcd 3266 (1992).

[239] *Amendment of Part 74 of the Commission's Rules With Regard to the Instructional Television Fixed Service, Notice of Proposed Rulemaking*, 8 FCC Rcd 1275 (1993).

[240] WCA Comments at 6-7.

[241] At its June 9, 1994 meeting, the Commission adopted three orders pertaining to wireless cable. One rule change permitted more streamlined ITFS application processing. *Amendment of Part 74 of the Commission's Rules With Regard to the Instructional Television Fixed Serv., Order & Further Notice of Proposed Rulemaking*, 9 FCC Rcd 3348. The second allowed all educational programming to be "loaded" onto a single ITFS channel, thus allowing the other three channels to be leased to the wireless operator on a full-time basis. *Amendment of Part 74 of the Commission's Rules Governing Use of the Frequencies in the Instructional Television Fixed Serv., Report & Order*, 9 FCC Rcd 3360. The third centralized the processing and regulatory jurisdiction over wireless cable in the Mass Media Bureau. *Amendment of Parts 0 and 1 of the Commission's Rules to Reflect a Reorganization of Multipoint & Multichannel Multipoint Dist. Serv. Regulation, Order*, 9 FCC Rcd 3661. As part of this administrative reorganization, the Commission has assembled a team of 20 engineers, attorneys and analysts to process the pending wireless cable applications and petitions.

[242] WCA Comments at 7.

[243] BERZINS, *supra* note 229, at 4-5.

homes without line-of-sight to receive service, recently has been developed.[244] If effective, this technology would increase the number of "homes seen" by wireless systems. It is unclear, however, whether signal boosting can be accomplished in most wireless systems on a cost-effective basis.[245]

88. Third, wireless operators complain that their operations are hampered by the fact that they cannot interconnect separately-owned buildings by wire, even if the wire only crosses private property.[246] WCA states that the interconnection of subdivisions, townhomes and trailer parks by wire is more efficient than interconnection by microwave, which requires the purchase of expensive equipment.[247] Accordingly, WCA contends that Congress's failure to extend the "private cable" exemption of the Communications Act[248] to interconnection of *separately*-owned buildings on private property is "one of the greatest impediments to competition."[249]

89. Finally, WCA has suggested that a potential impediment to the growth of wireless cable services is alleged anticompetitive behavior by cable operators.[250] For example, WCA described situations in which franchised cable operators may have induced local ITFS licensees to not lease their excess capacities to wireless cable operators.[251] The record does not contain the necessary evidence to determine how widespread those allegedly anticompetitive practices might be. However, to the extent that aggrieved parties believe that

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[244] Andrew Kreig, *Major Digital Initiatives, New Products Announced*, SPECTRUM (Newsletter of WCA) (July 1994) at 3; *See also* John Ramsey, *MMDS: The Advent of Latin American Pay TV; Method of Delivering Pay Television Programs*, SATELLITE COMM., Aug. 1993, at 17.

[245] TOWARD COMPETITION, *supra* note 132, at 133.

[246] In its *Definition of a Cable System, Report & Order ("Definition of a Cable System")*, 5 FCC Rcd 7638, *aff'd sub nom., FCC v. Beach Communications, Inc.*, ___ U.S. ___, 113 S. Ct. 2096 (1993), the Commission reversed its earlier position and concluded that a private cable system that interconnects by wire separately-owned or controlled buildings on private property is a "cable system," and therefore must obtain a franchise prior to offering service.

[247] WCA Comments at 18-19.

[248] Section 602 of the Communications Act exempts from the definition of a cable system "a facility that serves only subscribers in 1 or more multiple dwellings under common ownership, control or management, unless such facility or facilities us[e] any public right-of-way." 47 U.S.C. § 522(7)(B).

[249] *Id.*

[250] WCA Comments at 22-26; People's Choice Comments at 3.

[251] WCA Comments at 22-26.

such conduct violates Commission rules, their concerns may more properly be addressed in an appropriate complaint before the Commission, rather than in this *Report*.

90. Overall, it appears that two of the wireless cable industry's most significant problems, lack of capital and insufficient channel capacity, are being addressed. First, the program access provisions of the 1992 Cable Act appear to have given wireless operators the credibility to raise money in the public debt and equity markets, thereby easing the financial difficulties experienced by many wireless systems.[252] Second, the combination of improved Commission licensing and the use of digital compression is expected to alleviate wireless cable's channel capacity problem in the near future. The progress in these two areas has led some analysts to forecast continued growth for this industry. One industry analyst predicts that the wireless industry will serve 800,000 subscribers by the end of 1994, and 3.2 million subscribers by the year 2000.[253] That report also contained an estimate that the subscriber total will be drawn from approximately thirty-seven million homes capable of receiving wireless cable,[254] which would mean that wireless cable services would be subscribed to by 8.7% of the households to which it is available.

4. Satellite Master Antenna Television Systems (SMATV)

91. SMATV system operators (also known as "private cable systems") are MVPDs that serve residential, multiple-dwelling units ("MDUs"), and various other buildings and complexes. A SMATV system offers, in general, the same type of programming as a cable system, and the operation of a SMATV system, in large part, resembles that of a cable system -- a satellite dish receives the programming signals, equipment processes the signals, and wires distribute the programming to individual dwelling units. The primary difference between the two is that SMATV systems typically are unfranchised, stand-alone systems that serve a single building or complex, or a small number of buildings or complexes in relatively close proximity to each other. However, SMATV operators are increasingly using microwave facilities to interconnect properties spread over a metropolitan area.

92. Currently, one industry source estimates that there are approximately 3000 to 4000 SMATV systems operating nationwide.[255] As of August 15, 1994, approximately one

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[252] *Id.* at 2-3.

[253] *Critical Mass*, *supra* note 216, at 1. Another analyst believes that wireless cable will serve four million customers by 2000. BERZINS, *supra* note 229, at 1.

[254] A total of 37 million homes would represent approximately 40% of all homes in the United States. TOWARD COMPETITION, *supra* note 132, at 150.

[255] Letter dated Aug. 12, 1994 from Deborah C. Costlow, Esq., counsel to various private and wireless cable operators, to Cable Services Bureau staff ("Costlow Letter").

million subscribers were served by SMATV systems.[256] It is projected that by the end of 1994 there will be approximately 1.03 million subscribers to SMATV systems in MDUs, and over 1.10 million such subscribers by the end of 1995.[257]

93. Instances of SMATV service to MDUs and other buildings and complexes include the following:

- Liberty Cable Corporation ("Liberty Cable") operates private cable systems in Manhattan, New York, competing head-to-head with the incumbent franchised cable systems operated by Time Warner. According to its comments, Liberty Cable serves approximately 20,000 subscribers, and currently is adding approximately 1000 new subscribers each month.[258] Liberty Cable claims that it offers its services at approximately one-half the price of Time Warner.[259] Liberty Cable also comments that it has expanded the scope of its operations through use of an 18 GHz microwave network, which links its facilities without the need to use public rights-of-way.[260]

- MSE Cable Systems, Inc. ("MSE") provides SMATV service to MDUs and mobile-home parks in Southeast Michigan. MSE reportedly has grown from four systems passing approximately 2000 homes to thirty systems passing approximately 16,000 homes. It is suggested that MSE began serving its mobile-home park subscribers at a time when no franchised cable operators offered service to those locations, and thus developed its business by filling the need for video programming service in those locations.[261]

- Cable Plus, headquartered in Bellevue, Washington, operates SMATV systems in nine states, mostly in the west. In five years, it has grown

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[256] *Cable & Pay TV Census -- August,* MARKETING NEW MEDIA, Aug. 15, 1994.

[257] *Id.* at 4.

[258] Liberty Cable Comments at 2, nn.2, 7.

[259] *Id.* at 7-8.

[260] *See Amendment of Part 94 of the Commission's Rules to Permit Private Video Distribution Systems of Video Entertainment Access to the 18 GHz Band, Report and Order*, 6 FCC Rcd 1270 (1991).

[261] Costlow Letter, *supra* note 255, at 2.

from 8 systems passing approximately 2500 homes, to approximately 200 systems passing approximately 50,000 homes.[262]

- OpTel, Inc. has been operating SMATV systems since November, 1993. OpTel provides SMATV service to more than 330 properties, passing more than 105,000 households and serving more than 41,000 subscribers, in the Los Angeles, San Diego, Houston, Phoenix and the Dallas-Ft. Worth metropolitan areas. OpTel reportedly makes extensive use of 18 GHz microwave links to connect the facilities it serves, and also uses other delivery technologies, including coaxial and fiber optic cable. It is reported that 25% of OpTel's customers receive at least fifty-four channels, and the company expects to upgrade most of its remaining systems to provide similar channel capacity.[263]

- MaxTel Cablevision has SMATV operations in twenty-five states. Originally formed as a subsidiary of a real estate development company, MaxTel now serves approximately 280 properties. Its systems pass nearly 85,000 households and have 42,000 subscribers.[264]

94. SMATV operators may have the ability to offer lower prices than can wired cable operators for substantially the same services. Indeed, it is suggested that some SMATV operators may set their rates by looking to the rates charged by cable incumbents as guidelines and offering certain discounts from the cable rates.[265] It has also been reported that SMATV systems charge lower rates than franchised cable operators for premium services, with such price differences ranging from $1.00 per channel to an overall sixty percent discount.[266] One commenter suggests that SMATV operators are able to offer lower prices because cable systems are prohibited by Commission rules from engaging in price competition for a particular MDU where a SMATV system operates.[267]

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[262] *Id.*

[263] *Id.* at 2-3.

[264] *Id.* at 3.

[265] *Id.* at 2.

[266] *Id.*

[267] *See* Time Warner Comments at 25-26. Section 623(d) of the Communications Act requires a cable operator to have a uniform rate structure throughout the area served by its cable system. 47 U.S.C. § 543(d). In its *1993 Rate Report & Order,* the Commission observed that cable systems often offer bulk discounts to subscribers in MDUs, and expressed a desire that bulk discounts not be used as a means of displacing competition from alternative MVPDs, such as SMATV operators. *1993 Rate Report & Order* ¶ 424, 8 FCC Rcd at 5898.

(continued...)

95. On the other hand, regulatory barriers may artificially raise the cost of operating SMATV systems. First, where a SMATV system uses wires to connect separately-owned buildings, even though no public rights-of-way are crossed, a SMATV system is considered to be a "cable system" under the Communications Act, thereby requiring the operator to obtain a local franchise.[268] As is the case with wireless cable operators,[269] the statutory definition of "cable system" may thus have the unintended effect of raising the costs of SMATV operators, thereby having a negative effect on competition.

96. Moreover, SMATV operators contend that cable operator conduct under the Commission's cable home wiring rules has a chilling effect on competition.[270] Those rules, require, *inter alia*, that cable operators provide subscribers with the opportunity to acquire cable home wiring before the cable operator removes it from the premises after termination of service.[271] One SMATV operator argues that under these rules, it is unable to connect a subscriber that switched from the cable operator's services until after the cable operator disconnects and removes its equipment.[272] As a result, this SMATV operator contends that potential subscribers are dissuaded from switching to SMATV from their existing cable company.[273] However, it is unclear from this record whether these types of concerns reflect anticompetitive abuses, which can be remedied by changing the Commission's home wiring

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[267](...continued)
To prevent cable operator abuse, the Commission's regulations require that all similarly sized MDUs in a franchise area receive "the same bulk discount rate structure," and that the cable operator be able to demonstrate that it receives some economic benefit from offering the discount. *Id. See also Implementation of the 1992 Cable Act: Rate Regulation & Buy-Through Prohibition, Third Order on Reconsideration*, 9 FCC Rcd 4316 (1994).

[268] *See Definition of a Cable System*, 5 FCC Rcd 7638; Communications Act, §§ 602(5-7), 621(b)(1), 47 U.S.C. §§ 522(5-7), 541(b)(1).

[269] *See supra* ¶ 88.

[270] *See, e.g.*, Liberty Cable Comments at 16-18.

[271] 47 C.F.R. § 76.802. The purpose of the cable home wiring rules is to avoid the disruption from having the wire removed after service is terminated and to allow subscribers to utilize the wires with competing MVPDs, thereby facilitating competition from these entities. *Implementation of the 1992 Cable Act, Cable Home Wiring, Report & Order*, 8 FCC Rcd 1435 (1993), *recon. pending.*, MM Docket No. 92-260. The Commission currently has before it a petition to initiate a rulemaking to determine how cable subscribers may have access to existing cable home wiring for the delivery of competing and complementary services. *Joint Petition for Rulemaking on Cable Television Wiring, Public Notice*, 8 FCC Rcd 8184 (1993).

[272] Liberty Cable Comments at 16-17.

[273] *Id.*

rules, or merely reflect the competitive nature of the marketplace.[274] The Commission will address home wiring issues when it rules on the petitions for reconsideration that are now pending.

5. *Broadcast Television Service*

97. Broadcast television stations are, and always have been, significant suppliers in the market for delivered video programming. In the 1993-94 season, ABC, CBS, NBC and Fox maintained a combined 72% share of prime-time viewers.[275] Even among those households subscribing to cable, retransmitted broadcast channels had a 46% prime time viewing share in the 1992-93 season, while retransmitted independent broadcast and public television stations maintained 17% and 3% shares respectively.[276] Therefore, two-thirds of all cable households watching television delivered by cable in the 1992-93 season were watching a retransmitted broadcast channel. Moreover, more than one-third of all households that could subscribe to cable service elected not to do so.[277] Accordingly, it would appear that for at least some viewers, broadcast television service satisfies their demand for video programming.[278]

98. Moreover, broadcast television remains an important outlet for the distribution of local news, public affairs, and sports programming. As the Commission found earlier this year, high profile sporting events like the Super Bowl, the World Series, the NBA Championships, and the NCAA basketball championships remain on broadcast television.[279]

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[274] *See* Time Warner's Reply Comments at 25 (arguing that there is nothing illegal about removing its own property from an MDU or terminating its own lines). Some of Liberty Cable's other concerns in its comments can be characterized more appropriately as common law claims for unfair competition rather than violations of the Communications Act. *See, e.g.*, Liberty Cable Comments at 18 (allegation that Time Warner has engaged in false and disparaging advertising against it). Such allegations should not be addressed to the Commission; perhaps they might be brought before a court of competent jurisdiction.

[275] NCTA Comments at 19.

[276] *Viewing Shares Broadcast Years 1983/1984 - 1992/1993*, CABLE TELEVISION DEVELOPMENTS (National Cable Television Assoc.), Apr. 1994, at 5-A (citing A.C. Nielsen Co. statistics).

[277] Of the 92.9 million homes passed by cable at the end of 1993, 57.4 million subscribed to basic cable services. *See* Appendix C, Table 1.

[278] On the other hand, there are various reasons why some households might prefer not to subscribe to cable service, including financial ones.

[279] *Implementation of Section 26 of the 1992 Cable Act -- Inquiry into Sports Programming Migration, Final Report* ¶ 167, 9 FCC Rcd 3440, 3501 (1994).

99. Finally, it has recently been reported that "[d]emand for television stations is at one of its highest levels in years."[280] First-quarter 1994 profits of broadcast television station group owners rose by at least 30%, fueled by increased advertising revenues.[281] In addition, Fox has successfully launched what has been termed an "emerging" fourth broadcast network,[282] and it is widely reported that Time Warner and Paramount, companies with cable television affiliations, are also seeking to create broadcast networks.[283] There are also more broadcast stations today than ten years ago, when the 1984 Act was passed. Between 1984 and 1994, the number of television stations operating in the United States grew from 1149 to 1518, which represents a 32% increase in the number of broadcast signals available to the public.[284]

100. Despite the increases in broadcast television output noted above, the number of broadcasting outlets available to consumers has not kept pace with the virtual explosion of programming alternatives available on cable television. In the last decade, the number of national cable video networks increased from forty-seven to ninety-nine, an increase of 110%.[285] The channel capacity of cable systems has also grown dramatically.[286] Cable systems have responded successfully to consumer demand in the last decade, as the market penetration of the cable industry has increased from 43.7% in 1984, to 62.5% in 1994.[287]

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[280] Julie A. Zier, *TV Buyers Agree: It's a Seller's Market*, BROADCASTING & CABLE, Apr. 25, 1994, at 22.

[281] Geoffrey Foisie, *Good Revenue Gains Spark Dazzling Profit Growth*, BROADCASTING & CABLE, Apr. 25, 1994, at 18.

[282] *Evaluation of the Syndication & Fin. Interest Rules, Memorandum Opinion & Order*, 8 FCC Rcd 3282, 3331-35 (1993); *Memorandum Opinion and Order on Reconsideration*, 8 FCC Rcd 8270, 8303 (1993), *appeal denied*, *Capital Cities/ABC, Inc. v. FCC*, 29 F.3d 309 (7th Cir. 1994).

[283] Joe Flint, *Clash of the Titans, Fifth-Network Style,* BROADCASTING & CABLE, Dec. 20, 1993, at 38-39; Tim Jones, *TV Merger Talks Just A Start; Off-Camera Maneuverings in the TV and Movie Industries Could Amount to a Fundamental Reordering of the Entertainment Power Structure*, CHI. TRIB., Sept. 2, 1994, at 1 (Business).

[284] BROADCASTING & CABLE YEARBOOK 1994 ("1994 YEARBOOK") C-218 (R.R. Bowker, pub. 1994).

[285] *National Cable Video Networks by Type of Servs. 1976-1993*, CABLE TELEVISION DEVELOPMENTS, (National Cable Television Assoc.), Apr. 1994, at 7-A.

[286] *See* Appendix C, Tables 2 & 3.

[287] *Basic Cable 1975-1983*, CABLE TELEVISION DEVELOPMENTS (National Cable Television Assoc.), Apr. 1994, at 2-A.

101. The Commission found in 1991, that the availability of over-the-air broadcast signals, can, under certain circumstances, have some constraining effect on cable system conduct.[288] However, cable systems offer a "steadily-expanding complement of specialized program services," which can increasingly meet consumer demand for more video programming choices.[289] Accordingly, any constraining effect appears to decrease to the point where the menu of available broadcast signals is insufficient to constrain cable market power. Most recently, the Commission examined the competitive effect of broadcast stations on cable rates in connection with the *1994 Rate Report & Order*. There, the Commission's statistical analysis was consistent with a finding that the availability of six or more local broadcast stations does not constrain cable rates.[290]

102. Advances in broadcast technology and regulatory policy might allow for multichannel broadcasting of digitally-compressed signals.[291] The Commission has recognized that multiplexed, multichannel broadcast signals could provide a competitive check on the exercise of market power by cable systems in the future. In its *1993 Rate Report & Order*, the Commission stated that "should digital compression or other technology advance to the point that a single broadcaster in a community were able to offer programming comparable to that offered by a cable system, such a broadcaster might well be deemed an MVPD

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[288] *1991 Effective Competition Report & Order* ¶ 22, 6 FCC Rcd at 4549. The competitive relationship between broadcast stations and cable systems is complicated by the fact that the signals of most local broadcast stations are retransmitted by cable systems. On the one hand, cable operators and broadcasters are direct competitors in certain markets, such as the market for local spot advertising. On the other hand, the programming of local broadcast stations is an important input for cable systems, which enhances the value of cable services offered to subscribers. Cable systems also provide an additional mode of distribution for broadcasters, which supplements over-the-air transmission.

[289] *1990 Cable Report* ¶ 69, 5 FCC Rcd at 4971-72. In Section III.A of this *Report*, the Commission reviews its prior findings regarding the constraining effect broadcast availability might have on cable system pricing.

[290] *1994 Rate Report & Order*, *supra* note 50, Appendix C at 21 & n.54.

[291] *See* TOWARD COMPETITION, *supra* note 132, at 141-47.

effectively competing with the cable operator."[292] The Commission reaffirms that possibility here.

C. Other Actual or Potential Competitors

1. Local Exchange Carrier (LEC) Entry

103. As noted in the *NOI*, the participation of local exchange carriers ("local telephone companies" or "LECs") in the multichannel video marketplace was not included in the competition analysis of the *1990 Cable Report* because it was deemed unlikely to occur in the near term.[293] At that time, local telephone companies were prohibited by statute and federal regulation from providing video programming directly to subscribers within their service areas.[294] While LECs were permitted to provide video programming outside their

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[292] *1993 Rate Report & Order* ¶ 24, 8 FCC Rcd at 5652-53 (footnotes omitted); *see also* NCTA Comments at 18. There are, however, indications that television broadcasters, if permitted to provide multiple channels of programming over the same 6-MHz signal, might seek to provide services other than the multichannel video services typically associated with cable television operators and their competitors. *See, e.g.*, John D. Abel, *Next Generation Media -- Convergence and Multimedia Broadcasting* 6-7 (Exec. V.P. National Association of Broadcasters May 1994) (stating that applications of digitalized broadcast signals could include: (1) a single high definition television ("HDTV") signal of extremely high quality; (2) an HDTV signal of lower quality and data about that signal that explains more about the program, provides additional camera angles and other program information; (3) multiple full motion video signals (three-to-five per 6 MHz broadcast channel); and (4) a video signal and separate bit streams devoted to receivers connected to telecopiers, computers, personal digital assistants, special audio receivers, pagers, separate non-video bit streams for e-mail, paging, PDAs, utility load management, data transmissions and telecopiers.)

[293] *1990 Cable Report* ¶ 108, 5 FCC Rcd at 5019.

[294] Section 613(b) of the Communications Act, 47 U.S.C. § 533(b), prohibits a common carrier from providing video programming directly to subscribers in its telephone service area, either directly, or indirectly through an affiliate owned by, operated by, controlled by, or under common control with the common carrier. That statutory provision is referred to as the cross-ownership ban. In 1990, the Commission further restricted LECs to strict carrier-user relationships with cable operators, except in rural areas where telephone companies were permitted to provide video programming to subscribers within their service areas. *See* 47 C.F.R. §§ 63.54, 63.58 (1990).

In addition to the restrictions contained in the Commission's rules, the court-ordered divestiture agreement under which AT&T divested its local exchange service business (the Modified Final Judgement or "MFJ") restricts the Bell Operating Companies' ("BOCs") ability to provide video programming services because its terms prohibit BOCs from

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telephone service areas, and channel service to unaffiliated cable operators within their service areas, few LECs participated in such ventures.[295]

104. Since 1990, the Commission has adopted orders easing the regulatory restrictions and creating a "video dialtone" ("VDT") framework for LEC participation in the multichannel video distribution marketplace consistent with the statutory prohibition.[296] That VDT framework, along with technological advances, has spurred increased video-related activity by LECs, including several market and technical trials and twenty-four applications for permanent authority covering over 8.5 million homes.[297] These applications, taken together, constitute a promising source of competition to cable operators for the multichannel distribution of video programming.

105. In this section of the *Report,* the Commission reviews: (1) the regulatory and statutory framework for LEC participation in the provision of video programming to subscribers; (2) the technology involved in deployment of a VDT system; (3) the status of the authorized market and technical trials; and (4) the applications for permanent VDT authorizations. The Commission also discusses the technology and architecture of the systems, and the regulatory and reporting issues that may affect the potential of this technology to provide competition to cable.

106. Regulatory Framework for LEC Participation in Video Transport Services. Under the VDT regulatory framework adopted by the Commission in 1992, a LEC may make available, on a nondiscriminatory common carrier basis, a platform capable of providing nondiscriminatory access to multiple video programmers and of delivering video

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[294](...continued)
providing inter-local access and transport area ("interLATA") services, and from manufacturing telecommunications equipment. *United States v. AT&T,* 552 F. Supp. 131 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States* 460 U.S. 1001 (1983).

[295] *Cf. Pacific Bell*, 60 RR2d 1175 (CCB 1986), *recon. granted in part*, 2 FCC Rcd 265 (1987), *aff'd, Century Fed., Inc. v. FCC*, 846 F.2d 1479 (D.C. Cir. 1988) (channel service); *General Tel. Co.*, 4 FCC Rcd 5693, *rev'd sub nom., National Cable Television Assoc., Inc. v. FCC*, 914 F.2d 285 (D.C. Cir. 1990), *on remand, General Tel. Co.*, 8 FCC Rcd 8178, *admin. stay denied*, 8 FCC Rcd 8753 (1993), *petition for review pending, GTE Cal. v. FCC* No. 93-70924 (9th Cir.), *and judicial stay granted* (9th Cir. Jan. 5, 1994) ("good cause" waiver of cross-ownership ban).

[296] The Commission began its re-examination of the telephone-cable company cross-ownership restrictions with a notice of inquiry in 1987. *Telephone Co.-Cable Television Cross-Ownership Rules, Sections 63.54-63.58, Notice of Inquiry*, 2 FCC Rcd 5092 (1987).

[297] Appendix D of the *Report* contains a list of LEC applications for trial and permanent service, and Appendix E of the *Report* contains detailed information about the trials, and descriptions of the services proposed in the applications for permanent service.

programming and other services to end users within its local telephone service area.[298] The LEC may also provide additional enhanced and non-common carrier services to customers of the common carrier platform.[299] In fashioning the VDT scheme, the Commission determined that the statutory cross-ownership restriction applies only to LECs within their local exchange service areas, and not to interexchange carriers.[300] In addition, neither a LEC offering VDT service, nor its programmer-customers, is required to obtain a local cable television franchise.[301] A LEC may own up to five percent of a video programmer, and participate in certain non-ownership affiliations with video programmers that use the basic platform.[302] Authorization pursuant to Section 214 of the Communications Act ("Section 214 authorization") is required for LEC provision of VDT service, and the Commission has established safeguards to prevent discrimination and cross-subsidization.[303]

107. As noted above, a LEC may also participate in video transport service through the provision of traditional channel service within its telephone service area to unaffiliated

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[298] *Telephone Co.-Cable Television Cross-Ownership Rules, Sections 63.54 - 63.58, Further Notice of Proposed Rulemaking, Second Report & Order, Recommendation to Congress, & Second Further Notice of Proposed Rulemaking ("Telco-Cable Second Report & Order")* ¶ 2, 7 FCC Rcd 5781, 5783 (1992), *recon. pending, and appeal pending sub nom., Mankato Citizens Tel. Co. v. FCC,* No. 92-1404 (D.C. Cir. Aug. 26, 1994). Under the VDT framework, multiple service providers, or programmer-customers, acquire capacity from the LEC on a tariffed basis to provide video programming and other services to end users.

[299] *Id.*

[300] *Telephone Co.-Cable Television Cross-Ownership Rules, Sections 63.54 - 63.58, Further Notice of Proposed Rulemaking, First Report & Order & Second Further Notice of Inquiry ("Telco-Cable First Report & Order")*, ¶ 46, 7 FCC Rcd 300, 323 (1991), *recon. granted in part*, 7 FCC Rcd 5069 (1992), *appeal denied sub nom. National Cable Television Assoc. v. FCC*, ___ F.3d ___, No. 91-1649 (D.C. Cir. Aug. 26, 1994).

[301] *Telco-Cable First Report & Order, on reconsideration*, 7 FCC Rcd 5069. Bell Atlantic reportedly recently announced its intention to contribute funds to municipal governments in areas where it constructs and operates VDT service. *See Telcos Approach Locals on Video Dialtone*, BROADCASTING & CABLE, Aug. 8, 1994, at 12.

[302] *Telco-Cable Second Report & Order,* 7 FCC Rcd 5781. In adopting relaxed ownership and non-ownership rules, the Commission determined that the statutory restriction of 47 U.S.C. § 533(b) was meant to be less restrictive than the Commission's prior rules. *Id.* ¶ 66.

[303] *Id.*

cable systems.[304] The VDT framework does not affect this traditional service offering. Consistent with the statutory restriction, a LEC is also permitted to own and operate cable facilities outside its service area, and to own video programming.[305]

108. The Commission has recommended that Congress repeal the telephone company-cable company cross-ownership prohibition and permit LECs to provide video programming directly to subscribers within their service areas.[306] The cross-ownership restriction was instituted by the Commission in 1970, following a series of proceedings in which the Commission found that telephone companies denied access or provided discriminatory access to cable systems to utility poles necessary for cable distribution.[307] Certain aspects of the regulatory restriction were codified by Congress in the 1984 Cable Act.[308] In 1993 the U.S. District Court for the Eastern District of Virginia held the cross-ownership prohibition unconstitutional as applied to Bell Atlantic in its service areas; in 1994 US West obtained a similar ruling in the U.S. District Court for the Western District of Washington.[309] The other Regional Bell Operating Companies ("RBOCs") have each filed

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[304] *See, e.g., Pacific Bell*, 60 RR2d 1175 (CCB 1986), *recon. granted in part*, 2 FCC Rcd 265 (1987), *aff'd sub nom. Century Fed., Inc. v. FCC*, 846 F.2d 1479 (D.C. Cir. 1988); *Pacific Bell II*, 6 FCC Rcd 688 (1991).

[305] For example, within the past year: Southwestern Bell acquired two operating cable systems in the Washington D.C. metropolitan area from Hauser Communications; US West purchased several cable systems in the Atlanta, Georgia area; and BellSouth entered into an agreement to acquire a 22.5% interest in Prime Cable, a Texas-based MSO. *See Telco Television Update*, BROADCASTING & CABLE, Aug. 15, 1994, at 7. With regard to LEC ownership of video programming, it is noted that US West holds an interest in Time Warner Entertainment, and NYNEX owns part of Viacom Inc. *Id.*; *see also Time Warner Entertainment Company, L.P. & US West Communications, Inc.*, 8 FCC Rcd 7106 (1993) (temporary waiver of the cross-ownership rules granted to Time Warner for 18 months to divest cable systems within US West's service areas).

[306] *Telco-Cable Second Report & Order*, 7 FCC Rcd 5781.

[307] *Applications of Tel. Cos. for Section 214 Certificates for Channel Facilities Furnished to Affiliated Community Antenna Television Sys.*, 21 FCC 2d 307 (1970), *appeal denied*, *General Telephone of the Southwest v. U.S.*, 449 F.2d 846 (5th Cir. 1971).

[308] Communications Act § 613(b), 47 U.S.C. §533(b)(1984).

[309] *Chesapeake & Potomac Tel. Co. v. United States*, 830 F. Supp. 909 (E.D. Va. 1993), *Amended Final Order*, No. 92-1751-1 (Oct. 7, 1993), *appeal docketed*, Nos. 93-2340, 93-2341 (4th Cir., Oct. 15, 1993) (Section 533(b) held unconstitutional as applied to Bell Atlantic within its service areas); *US West, Inc. v. United States*, No. C93-1523R (W.D. Wa. June 14, 1994), *appeal docketed*, No. 94-35775 (9th Cir., August 3, 1994) (Section 533(b) held unconstitutional as applied to US West within its service areas). *But see Marsh Media,*

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similar challenges to the constitutionality of the cross-ownership ban in federal district courts in their service areas, as has the United States Telephone Association on behalf of its members.[310]

109. Overview of LEC Applications for VDT trials and for Permanent Services. Since adoption of the VDT regulatory framework, the Commission has granted applications by five different LECs for technical and market trials.[311] Five additional applications for new or expanded trials are pending before the Commission. The cost estimates for the various trials range from $2.5 million to $11 million and cover between 250 to 2000 households per trial.[312] Twenty-four applications for permanent commercial VDT service have also been filed with the Commission, including applications by six of the seven RBOCs, as well as GTE.[313] These applications propose VDT platforms using various distribution technologies which, if granted, would provide service to over 8.5 million homes.

110. In July 1994, the first permanent Section 214 authorization was granted to New Jersey Bell for Dover Township.[314] Pursuant to that grant, New Jersey Bell is authorized to construct and operate a system to provide VDT service to approximately 38,000 homes using a FTTC architecture, with coaxial cable and copper wire for the final link to the home and providing initial digital capacity of 64 channels, conditioned upon expanding capacity to 384 digital channels by January 3, 1995.[315] FutureVision of America, Corp., the initial programmer-customer, is limited to a maximum of 32 channels (half the initial channel

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[309](...continued)
Ltd. v. FCC, 798 F.2d 772 (5th Cir. 1986) (First amendment challenge to television-cable cross-ownership restriction of Section 533(b) held foreclosed by Supreme Court decision in *FCC v. National Citizens Committee for Broadcasting*, 436 U.S. 775 (1978), upholding television-newspaper cross-ownership rule).

[310] *United States Tel. Assoc. v. United States*, Case No. 1:94CV01961 (D.D.C., filed Sept. 12, 1994).

[311] *See* Appendix E.

[312] *See Application of US West Communications, Inc. for Section 214 Auth. to Provide VDT Servs. in Omaha, Neb. ("US West VDT Application")* ¶ 24 n.59, 9 FCC Rcd 184, 188 n.59.

[313] *See* Appendix E.

[314] *See Application of New Jersey Bell Tel. Co. for Section 214 Auth. to Provide VDT Servs. in Dover, N.J. ("New Jersey Bell VDT Application")*, 9 FCC Rcd 3677 (1994).

[315] New Jersey Bell predicts that 35% of the homes passed will become end-user subscribers. *New Jersey Bell VDT Application* ¶ 3, 9 FCC Rcd 3678.

capacity) during the six-month interim transition period from a 64 channel system to a 384 channel system.[316]

111. Reports on the status of the trials have been submitted by Bell Atlantic and NYNEX, and a tariff has been filed by Rochester Telephone. In other filings and comments in this proceeding, various LECs have proffered their views on the status of VDT and current technology.[317]

112. Technology and Architecture Issues. In addition to regulatory and legal constraints discussed above, technology has also played a role in restraining the entry of LECs into the multichannel video programming distribution marketplace. While an infrastructure owned by telephone companies currently exists for delivery of narrowband voice communications to most homes and businesses in the nation, that infrastructure is unable to transport and deliver multichannel video programming to multiple end users. Various techniques, technologies and architectures for delivering broadband video signals are currently being tested. Some of these include: optical digital loop carrier systems, fiber to the node ("FTTN"), fiber to the curb ("FTTC"), fiber to the home, hybrid fiber-coax networks ("HFC"), asynchronous digital subscriber line ("ADSL"), and various broadband switches. For a brief description of these technologies, see Appendix B.

113. Initially, US West asserts that analog-based transmission appears to be preferable to digital from the perspective of end user access and program availability.[318] However, analog channels impose capacity requirements that limit the expandability of VDT offerings.[319] NYNEX's report on the status of its VDT trial indicates that its trial platform provided sufficient analog channel capacity to accommodate all parties requesting direct

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[316] According to a recent trade press report, Cablevision Systems, Inc., the fifth largest MSO, has requested access to channel capacity on the Dover VDT platform. Kent Gibbons, *Cablevision Wants Piece of VDT Network*, MULTICHANNEL NEWS, Aug. 29, 1994, at 1; *Bell Atlantic VDT Plan Hit*, TELEVISION DIGEST, Aug. 29, 1994.

[317] The Bell Atlantic, Rochester Telephone and other reports and filings are summarized in Appendix E.

[318] *US West VDT Application* ¶ 7-8 nn. 18-19, 9 FCC Rcd at 188 nn. 18, 19. That preference is likely attributable to the fact that nearly all television programming has been created in an analog format, and cable-ready television sets can display such programming without a set top converter box. It should be noted, however, that analog systems cannot economically be carried on fiber. *Cf.* JACK L. DEMPSEY, TELECOM BASICS 47 (1988).

[319] For example, the first phase of the NYNEX VDT trial utilizes an analog system: the platform, with 750 MHz of transport spectrum, can deliver 110 6-MHz NTSC format analog channels or a combination of 80 analog channels and more than 300 3.5-Mb/s MPEG format channels. *See* Rob Rockefeller, *Putting Video Dialtone to the Test in Manhattan,* TELEPHONY, June 13, 1994, at 46. *See* Appendix B for definitions of terms.

access to such channels, but was unable to provide sufficient stored access capacity.[320] GTE believes that compression capabilities will have a competitive impact beginning in 1995.[321] Other commenters assert that the limitations of analog may cease to be a constraint when the price of analog-to-digital conversion declines significantly and more programming is digitally encoded.[322] GTE predicts that digital compression will be readily available during 1995, and broadband switching sometime during 1996.[323]

114. The ability of LECs to use their existing infrastructure to offer video services may also play a role in the deployment of VDT as an effective competitor to cable. Just a few years ago, industry projections for upgrading the telephone infrastructure by installation of fiber optics suggested that VDT deployment could only be slated for the next century.[324] However, with new technologies and architectures, those projections have changed significantly. For example, ADSL technology and integrated HFC networks are both expected to speed deployment of VDT.[325] Bell Atlantic's report on the status of its technical trial notes that while technical difficulties were experienced with some of the prototype video decoders, ADSL is "proving to be a successful medium for delivery of voice, video and data services."[326] Rochester Telephone, however, notes that current ADSL technology is capable

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[320] *Six Month Compliance Report of NYNEX ("NYNEX Six Month Report")*, Attachment 2, at 5-6, Attachment 3, *Application of NYNEX for Section 214 Auth. to Provide VDT Servs. In New York City*, File No. W-P-C 6836 (filed July 15, 1994). With direct access, a VDT programmer-customer continually transmits programming over a particular channel. With stored access, the programmer-customer provides a data base of programming that the subscriber can access, similar to selecting a song from a juke box.

[321] GTE Comments at 13.

[322] *US West VDT Application*, ¶ 27 n.66, 9 FCC Rcd at 189 n.66.

[323] GTE Comments at 13.

[324] *See, e.g.*, HENRY GELLER, FIBER OPTICS: AN OPPORTUNITY FOR A NEW POLICY (1991). Such projections generally assumed fiber to the home was necessary to effectively transport video.

[325] Most of the applications for permanent VDT authorizations propose some type of HFC architecture. According to a recent FCC report, it is estimated that the interexchange carriers deployed 2.5 million fiber miles as of the end of 1993; the BOCs have deployed 6.3 million fiber miles; and all local operating companies have deployed over 7.2 million fiber miles. Jonathan M. Kraushaar, Fiber Deployment Update -- End of Year 1993 (May 1994) (available in reference room at the Federal Communications Commission, Common Carrier Bureau, Industry Analysis Division).

[326] *Six Month Compliance Report of Bell Atl. Co. ("Bell Atl. Six Month Report")*, *Application of Bell Atl. for Section 214 Auth. to Provide VDT Servs. in No. Va.*, File No. W-P-C 6834 (filed Sep. 27, 1993). ADSL is a form of signal compression that enables

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of delivering only one retransmitted broadcast signal to a customer, *i.e.*, end users are able to select only one programmer-customer at a time from the available service providers using the ADSL system.[327] GTE notes that information about customer satisfaction and the migration path for ADSL technology (*e.g.*, to accommodate High Definition Television ("HDTV")) are not known.[328] Bell Atlantic projects that recent innovations in encoding, compression and multiplexing technology are expected to permit delivery of "live" broadcast programming over copper loops beginning in 1995, and that digital pointcast capability using broadband switching technology will become generally available beginning in 1996.[329]

115. With respect to end-user concerns, NYNEX notes that tests of the hybrid fiber-coax architecture demonstrate that if two customers are served by the same drop, it is not possible for both customers to choose different programmers.[330] Nevertheless, NYNEX reports that the hybrid fiber-coax network is successfully delivering direct and stored access analog VDT services, and that the baseband analog switch is effectively delivering menu service and video and audio signals from multiple video information providers to the end users, who have access to interactive services. Switched access has not yet been introduced on the NYNEX analog platform because the analog format is not capable of managing sessions for video-on-demand applications.[331] In other contexts, however, GTE asserts that technology is currently available to provide enhanced video services packaging for consumers.[332]

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[326](...continued)
existing copper twisted pairs to carry one or more television signals, along with telephone service, to the subscriber. Bell Atlantic reported that distance ranges on the decoders -- 11,000 feet when used with 26 gauge wire -- were less than expected and that subscribers experienced problems with non-synched voice and video and video freeze frames with some decoders. It reports that the problems are with the decoders, not the ADSL system.

[327] *Application of Rochester Tel. Co. to Conduct a Market Test of VDT Servs. in Rochester, N.Y.* ¶¶ 7-8, DA Docket No. 94-275 (1994) (File No. W-P-C 6867 1994).

[328] GTE Comments at 12. GTE also contends that the competitiveness of ADSL systems cannot be validly compared to cable systems because cable operators are rapidly deploying hybrid fiber coax systems. *Id.*

[329] Bell Atlantic expects to begin testing digital pointcast capability in the Washington D.C. metropolitan area in 1995. Bell Atlantic Comments at 12.

[330] *See, e.g., NYNEX Six Month Report*, Attachment 6, at 4, WPC-6836. Providing separate subscriber drops to each customer solves this problem.

[331] *NYNEX Six Month Report*, Attachment 6, WPC-6836. Rather, NYNEX employs a "video juke box" to deliver stored and timeshifted video information provider programming to the limited base of interactive trial end-users, with VCR-like functionalities. *Id.*

[332] GTE Comments at 12.

116. Regulatory and Statutory Issues. LECs commenting in this proceeding assert that there are two reasons why VDT service has not yet proven itself as a viable competitor to cable service: (1) the statutory ban on the provision of video programming by LECs to subscribers in their own service area; and (2) the fact that the Commission has not yet granted most of the Section 214 VDT applications. The LEC commenters recommend: (1) repeal of the 1984 Cable Act's ban on LEC provision of video programming;[333] (2) expedition, streamlining or elimination of the Section 214 application process;[334] (3) continued resistance to the imposition of local franchise requirements on LECs;[335] and (4) regulatory parity with cable.[336] GTE asserts that adjustments in the rate regulation framework for the cable industry should correspond with relaxation of LEC price caps, such that both industries are provided incentives to compete on the basis of price and service.[337] As noted above, the Commission has recommended to Congress the repeal of the cable-telephone company cross-ownership ban, and is processing Section 214 applications to provide VDT service.

117. In addition to the hurdles to providing VDT service facing all LECs, the BOCs also must comply with the Modified Final Judgment ("MFJ"). As noted above,[338] the MFJ ban on BOC provision of interLATA services prohibits BOCs from receiving satellite or over-the-air video signals -- which is how cable systems typically receive most of their programming -- without obtaining a waiver of the MFJ. The interLATA ban could also prevent interLATA offering of enhanced gateway services.[339]

118. GTE asserts that the length of time it will take for video dialtone to become an alternative to cable will depend on the LECs' respective market entry rates. Most LECs have

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[333] Bell Atlantic Comments at 7; GTE Reply Comments at 3.

[334] Bell Atlantic Comments at 7-8; NYNEX Comments at 2-4; GTE Comments at 3 n.5, 11, Reply Comments at 3; US West Comments at 3; Ameritech Reply Comments at 3.

[335] Bell Atlantic Comments at 8; GTE Reply Comments at 3.

[336] Bell Atlantic Comments at 8-9; GTE Comments at 3; GTE Reply Comments at 3.

[337] GTE Reply Comments at 5.

[338] *Supra* note 294.

[339] *United States v. AT&T*, 552 F. Supp. 131. The MFJ prohibition on BOC provision of information services was lifted in 1993. *United States v. Western Elec. Co.* 767 F. Supp. 308 (D.D.C. 1991), *aff'd*, 993 F.2d 1572 (D.C. Cir. 1993), *cert. denied sub nom. Consumer Fed. of Am. v. United States*, ___ U.S. ___, 114 S. Ct. 487 (1993). However, BOCs are still currently prohibited from providing interLATA services and designing and manufacturing equipment. *See United States v. Western Elec. Co,*, 1989-1 Trade Cas. (CCH) ¶ 68,400 (D.D.C. 1990), *cert. denied sub nom., Bell Atl. Corp. v. United States*, 488 U.S. 1109 (1991).

announced deployment schedules of five- to ten-year periods.[340] Trade press reports suggest that the BOCs hope to make video-capable networks available to over twenty million homes by the turn of the century.[341]

119. Reporting Issues. In response to the questions posed in the *NOI* regarding appropriate means for assessing the future competitive impact of VDT, nearly all of the commenters argue that data gathered in the technical and marketing trials is highly confidential and proprietary and should not be disclosed to potential competitors; (2) that sufficient information pertaining to system location, subscriber base, channel capacity and pricing will be provided in tariff filings; and (3) that customer proprietary information should not be required to be publicly disclosed in the future.[342] Disclosure of the total number of homes passed by VDT systems is deemed appropriate by the commenters, however, so long as such data is provided on a zip code, or Metropolitan Statistical Area, or state-wide basis.[343] The LECs also assert that subscribership, program offering, and price information should be gathered from programmer-customers who lease transmission capacity on the VDT platforms.[344]

120. Conclusion. A number of issues remain unresolved with respect to the participation of LECs in the delivery of video programming. The regulatory framework for permitting LECs to construct and operate a common carrier VDT platform for the transmission of video programming and other services to end-users is under review by the Commission.[345] Moreover, legislation proposing, among other things, to eliminate the

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[340] For example, GTE states that it plans to expand VDT to 66 markets and 7 million homes within the next 10 years. GTE Comments at 12.

[341] *See, e.g., Telco Television Update*, BROADCASTING & CABLE, Aug. 15, 1994, at 7.

[342] Bell Atlantic Comments at 11; GTE Comments at 7; BellSouth Comments at 2-3; Ameritech Reply Comments at 4.

[343] GTE Comments at 5-6. GTE asserts that a requirement that data be collected and reported on the basis of cable franchise areas would be burdensome.

[344] Bell Atlantic Comments at 11; GTE Comments at 3-5; GTE Reply Comments at 3-4; BellSouth Comments at 3-4; Ameritech Reply Comments at 4. GTE asserts that if the statutory prohibition is lifted, LECs should still not be required to provide such information because it would be tantamount to collecting and reporting the data to competing programmers. GTE Comments at 8-9.

[345] The Commission's decision that neither LECs nor their programmer-customers are required to obtain a local franchise in order to provide video programming to end-users was recently affirmed by the D.C. Circuit. *National Cable Television Assoc. v. FCC*, ___ F.3d ___, No. 91-1649 (D.C. Cir. Aug. 26, 1994).

telephone company-cable company cross-ownership ban is pending before Congress.[346] As noted above, the VDT industry is in its initial planning and construction phases. In future reports, the Commission will further review the development of LEC provision of video programming and its status as a competitive alternative to cable.[347]

2. *Local Multipoint Distribution Service (LMDS)*

121. LMDS is a new technology, similar to MMDS, in which multiple channels of video programming are transmitted using high-frequency microwave channels in the 28 GHz band. Like MMDS, LMDS subscribers must have a special antenna that is located with a line of sight to the transmitter. Because of the propagation characteristics in this frequency band, LMDS requires multiple transmitters in "cells" with radii of three to six miles in order to cover a metropolitan area that could be covered by a single wireless cable transmitter.[348]

122. In 1991, the Commission authorized the Suite 12 Group to provide LMDS.[349] Operating as CellularVision of New York ("CVNY"), it operates its LMDS system in Brooklyn, New York, and provides forty-nine video channels, including two premium movie channels for $29.95 per month. CVNY states that a comparable package from local cable operators would cost $10-20 more per month. CVNY also claims that LMDS provides higher picture quality than is available with cable, and that LMDS could be used as a

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[346] S. 1822, 103d Cong., 2d Sess. (1994); H.R. 3626, 103d Cong., 2d Sess. (1994).

[347] *See, e.g.*, GTE Comments at 12. US West suggests that the Commission should exclude VDT from its annual report to Congress until it is commercially available. US West Comments at 3. Ameritech states that comparisons of the 55 million cable subscribers with the recently granted permanent VDT authorization for 38 thousand homes passed make it patently clear that there currently is no basis to gather meaningful information on the impact of VDT on the market for the delivery of video programming. Ameritech Reply Comments at 3.

[348] TOWARD COMPETITION, *supra* note 132, at 135.

[349] *Application of Hye Crest Management, Inc. for License Authorization in the Point-to-Point Microwave Radio Serv. in the 27.5 - 29.5 GHz Band & Request for Waiver of the Rules*, 6 FCC Rcd 332 (1991). After granting that authorization, the Commission received over 900 applications accompanied by petitions for waivers from entities seeking to provide similar services. The Commission instituted a formal rulemaking proceeding to determine whether the 27.5 - 29.5 Ghz band ("28 GHz band") should be redesignated in order to accommodate multichannel video service, among other proposed uses. *See Rulemaking to Amend Part 1 & Part 21 of the Commission's Rules to Redesignate the 27.5 - 29.5 GHz Frequency Band & to Establish Rules & Policies for Local Multipoint Distribution Service, Notice of Proposed Rulemaking, Order, Tentative Decision & Order on Reconsideration*, 8 FCC Rcd 557 (1993).

platform for telephony as well as video programming.[350] Moreover, CVNY predicts that LMDS will be capable of using digital compression technology whenever it becomes commercially available.[351] CVNY reportedly has "a few hundred" subscribers.[352]

123. In 1991, the Commission stated that while "it is still too early in the development of LMDS to reach firm conclusions on the treatment of LMDS providers as multichannel video programming distributors," the Commission will analyze LMDS providers "for purposes of the effective competition determination in a manner appropriate to the degree of video distribution services they provide."[353]

124. In response to proposals from parties who wish to provide services other than LMDS in the 28 GHz band, the Commission sought and received approval to conduct a negotiated rulemaking among interested parties.[354] One of these parties, Teledesic Corporation ("Teledesic"), which has filed an application with the Commission to provide FSS (fixed satellite service) in the 28 GHz band, submitted comments in this proceeding stating that LMDS would merely duplicate the video entertainment being provided by cable, MMDS, DBS and video dialtone offerings.[355] Teledesic also contends that LMDS has not yet proven its feasibility on a large scale, and therefore, that the Commission should not assume that LMDS could provide competition to cable.[356]

125. Because the Commission has not yet determined whether the 28 GHz band will be designated for use by LMDS operators, it is premature for the Commission to draw any conclusions in this *Report* regarding the feasibility of LMDS or the desirability of a particular outcome of the negotiated rulemaking. If the Commission ultimately concludes that LMDS is to be licensed in the 28 GHz band, LMDS will be included in future reports to Congress.

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[350] CVNY Comments at 3-4.

[351] Fred Dawson, *CellularVision Fights Off New LMDS Challenges,* MULTICHANNEL NEWS, July 11, 1994, at 47.

[352] Teledesic Reply Comments at 5.

[353] *1993 Rate Report & Order* ¶ 25, 8 FCC Rcd at 5653-54.

[354] *Rulemaking to Amend Part 1 & Part 21 of the Commission's Rules to Redesignate the 27.5 - 29.5 Frequency Band & to Establish Rules & Policies for Local Multipoint Dist. Serv., Second Notice of Proposed Rulemaking,* 9 FCC Rcd 1391 (1994).

[355] Teledesic Reply Comments at 2.

[356] *Id.*

3. Low Power Television (LPTV)

126. Low power television ("LPTV") refers to use of the VHF and UHF spectra pursuant to the regulatory scheme that was established by the Commission in 1982 as a means of increasing diversity in television programming and station ownership.[357] Although this service has been highly successful in meeting that objective, there is now interest in using LPTV channels to provide multichannel video service.

127. The Commission's rules specifically permit LPTV channels to be used for "subscription television,"[358] whereby a licensee charges subscribers a fee for the provision of one or more scrambled channels and the equipment needed to descramble the signal. Unlike a full-service television station, an entity may hold more than one LPTV license in a particular market.[359] Therefore, an LPTV operator can accumulate a number of channels in a single market to provide multichannel video service. However, the Commission is presently not accepting applications for new LPTV stations for service within 100 miles of the top thirty-six United States cities in order to preserve spectrum availability for the implementation of HDTV systems by full-service stations.[360]

128. Despite that partial application freeze, the Commission received a significant number of LPTV construction permit applications in April 1994. According to an industry report, the interest in obtaining LPTV licenses is the result of a growing interest in providing multichannel LPTV service, and may also have been enhanced by the fact that signal scrambling methods have become more economical and advanced.[361]

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[357] *An Inquiry into the Future Role of Low Power Television Broadcasting & Television Translators in the Nat'l Telecommunications Sys.*, 51 RR2d 476 (1982).

[358] 47 C.F.R. § 73.642(a)(2).

[359] 47 C.F.R. § 74.732(b).

[360] *See Notice of Limited Low Power Television/Television Translator Filing Window,* FCC Public Notice No. 41954 at 1, n.1 (March 3, 1994) (*"LPTV Public Notice"*). The Commission has recognized that LPTV stations have "secondary service status," and as such, must yield to new full-power station assignments for the provision of advanced television services, such as HDTV. *Advanced Television Systems & Their Impact on the Existing Television Broadcast Serv., Memorandum Opinion & Order, Third Report & Order, & Third Further Notice of Proposed Rulemaking* ¶¶ 35-39, 7 FCC Rcd 6924, 6951-6955 (1992) . The application freeze was imposed so as to avoid displacing new LPTV stations and minimize the extent to which LPTV service to the public is disrupted as advanced television systems come on line. *LPTV Public Notice* at 1-2, n.1.

[361] *Scrambled LPTV Service Expected To Grow, Offer Cable-Like Service,* COMMUNICATIONS DAILY, May 20, 1994, at 2; *LPTV Emulating Cable*, TELEVISION DIGEST, May 23, 1994, at 6.

129. The Commission is aware of at least one company that presently provides multichannel LPTV service. Reports indicate that Broadcast Services International, Inc. ("BSI") provides multichannel LPTV service to approximately 500 subscribers in Duluth, Minnesota and to 250 subscribers in nearby Ely, Minnesota.[362] BSI is reportedly focussing its efforts on uncabled rural areas,[363] and it is unclear to what extent BSI's service would be a competitive substitute for cable service.[364] Another possible LPTV site involves Selma, Alabama, where construction permits for multiple LPTV station assignments have been issued to a single applicant. In addition, many of the applications received in April 1994 are for multiple LPTV channel assignments, primarily for rural markets.

130. While multichannel LPTV services may eventually become available in many areas, the application freeze on new LPTV stations within 100 miles of the thirty-six largest United States cities and the spectrum needs of advanced television systems suggest that multichannel LPTV entry will likely be limited to smaller and mid-sized markets. In addition, it is unclear whether multichannel LPTV will enter the market as a competitor to cable, or as a substitute to cable service in largely uncabled areas.

4. Electric Utilities

131. Electric utility companies may provide another potential source for the delivery of video programming.[365] Some municipal electric utility companies are actively engaged in overbuilding privately-owned cable systems, or are presently contemplating such overbuilding.[366] As is the case with LEC provision of VDT services,[367] the need for appropriate safeguards to avoid cross-subsidization between regulated and video distribution businesses is an issue associated with entry by electric utility companies.

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[362] *See Scrambled LPTV, supra* note 361, at 3; Joel Schofield, *LPTV: Finding a place in Wireless Cable*, WIRELESS BROADCASTING MAGAZINE, March/April 1994, at 12.

[363] *Id.*

[364] One report suggests that multichannel LPTV will typically be limited to ten to twenty channels, and potentially thirty channels with signal compression. *LPTV Emulating Cable, supra* note 361, at 6. In contrast, over 95% of the nation's cable subscribers receive 30 or more channels. *See* Appendix C, Table 3.

[365] For purposes of this discussion, electric utilities are considered to include investor-owned utilities, municipal utility systems, and exempt public utility holding companies. *See* 15 U.S.C. § 79c. However, that group could substantially increase if Congress passes pending legislation that would permit registered public utility holding companies to diversify into telecommunications and other industries. S. 1822, 103d Cong., 2d Sess. (1994) (which will, *inter alia*, amend 15 U.S.C. § 79i if adopted).

[366] *See* TOWARD COMPETITION, *supra* note 132, at 22.

[367] *See infra* ¶ 106.

132. Electric utilities' interest in cable television is based on the potential for capitalizing on their existing rights of way, and from the potential for using "demand-side" load management capabilities for the distribution of video programming.[368] "Demand-side" management involves, *inter alia*, a utility's ability to control or limit increases in demand for electricity during peak hours, for example by controlling its customers' air conditioners or pool-heaters through the installation of a broadband communications link to each home.[369]

133. As discussed in Section III.B.1, *supra*, the GEPB (Glasgow Electric Plant Board) in Glasgow, Kentucky is an example of a utility currently providing cable service. GEPB's initial purpose in creating its fully-interactive communications and control systems was simply to find a better way to manage its distribution network, and to reduce energy costs to consumers by monitoring consumption.[370] In June 1989, GEPB began offering cable television service to all 13,000 of its customers in competition with the local cable operator, and it has since acquired fifty percent of the market for cable television service.[371]

5. Video Cassette Recorders (VCRs)

134. VCRs (video cassette recorders) are not "multichannel video programming distributors." However, the Commission noted in the *1990 Cable Report* that widespread ownership of VCRs allows many viewers to see over-the-air programs at times other than when they are broadcast, and also permits those viewers to choose pre-recorded tapes on a variety of subjects, giving them more control over both the programming they watch and the

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[368] TOWARD COMPETITION, *supra* note 132, at 23.

[369] *Id.* at 23-24. However, American Electric Power Co. recently committed to implement commercially a technology that allows existing household phone lines to handle some of the key cost-saving tasks that previously had been envisioned for techniques that rely on fiber/coaxial links to the home. The new technology is called "TranstexT" and allows the energy company to conduct demand-side management by sending very low data rate signals over existing telephone connections. According to a trade press article, the use of this technology "could take utilities out of the broadband communications equation for some time to come." Fred Dawson, *Utilities Debate Role in Broadband Networks,* MULTICHANNEL NEWS, July 18, 1994, at 46; *see also AEP Plans to Install 25,000 Residential Energy Management Systems by 1997*, ELECTRIC UTILITY WEEK'S DEMAND-SIDE REPORT, Mar. 31, 1994, at 1; Ron Lietzke, *AEP to Help Customers Cut Bills*, COLUMBUS DISPATCH, Mar. 30, 1994, at F1.

[370] TOWARD COMPETITION, *supra* note 132, at 23 (*citing* Bob Bruce, *The Lure of Fiber Optics,* PUBLIC POWER, Sept.-Oct. 1993, at 16, 18).

[371] *Push by Municipal Utilities*, COMMUNICATIONS DAILY, Jan. 25, 1994, at 4; *Pressure Growing to Make Electric Utilities Major Players in NII*, WASHINGTON TELECOM WEEK, Jan. 28, 1994, at 23.

time they watch it.[372] The evidence in that proceeding demonstrated that VCR penetration had grown dramatically, reaching a penetration level of 72% in 1990, up 30% from 1986. Moreover, the Commission found that nationwide revenues from the sale and rental of video cassettes exceeded the revenues for basic cable service. Therefore, the Commission concluded that high VCR penetration levels and video cassette rentals, combined with broadcast or other over-the-air video delivery systems, offer an alternative that may act as a partial substitute for cable services.[373]

135. Since the *1990 Cable Report* was released, VCRs have become still more prevalent. Time Warner states that by the end of 1993, there were approximately 80.5 million households with VCRs, which compares to approximately 57 million cable households at that time.[374] Although those 80.5 million households with VCRs would account for nearly 84% of all television households in the United States, a study conducted by the Commission following its release of the *1990 Cable Report* found that VCRs are more properly categorized as competitors of premium or pay-per-view cable programming, rather than of cable services generally.[375]

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[372] *1990 Cable Report* ¶¶ 109-10, 5 FCC Rcd at 5019-20.

[373] *Id.*

[374] Time Warner Comments at 14 n.17 (*citing* KAGAN MEDIA INDEX at 14).

[375] *See* FLORENCE SETZER & JONATHAN LEVY, BROADCAST TELEVISION IN A MULTICHANNEL MARKETPLACE 108 (Federal Communications Commission, Office of Plans and Policy, OPP Working Paper Series, June 1991).

IV.
MARKET STRUCTURE CONDITIONS AFFECTING COMPETITION

136. In this section of the *Report*, the Commission discusses the status of horizontal concentration and vertical integration in the cable television industry, and the competitive effects of that concentration and integration. In brief, the Commission finds that horizontal concentration has increased moderately since it released the *1990 Cable Report*. Vertical integration among programmers and cable operators, on the other hand, has not changed significantly. As part of its responsibility for implementing the 1992 Cable Act, the Commission has adopted and enforced rules to mitigate the anticompetitive effects of such integration on entry of new competitors. Those rules appear generally to be effective in ensuring that those new competitors can gain access to programming produced by vertically-integrated cable companies.[376] Finally, the Commission discusses in the concluding paragraphs of this section certain technological developments that have the potential to change the structure of the industry.

A. Horizontal Concentration In The Cable Industry

137. In the *1990 Cable Report,* the Commission noted that horizontal concentration in the cable industry had significantly increased on a nationwide basis since the passage of the 1984 Cable Act. The Commission concluded that horizontal integration had not only "brought substantial benefits to American consumers, but also has added potential for certain anticompetitive conduct."[377] The benefits included more efficient production as a result of certain economies of scale, and the creation of a pool of capital for investment in programming.[378] The potential anticompetitive effects, on the other hand, included the danger that the larger MSOs would use their size to "extract unreasonable concessions from program suppliers and to unfairly restrain competition from alternative distribution services."[379] The Commission did not express an opinion in the *1990 Cable Report* as to whether the observed increase in horizontal integration was desirable. The Commission did state, however, that it intended to continue monitoring changes in concentration.[380]

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[376] Appendix F contains descriptions of program access cases that the Commission has resolved through September 19, 1994.

[377] *1990 Cable Report* ¶ 13(5), 5 FCC Rcd at 4972.

[378] *Id.* ¶¶ 82-84, 5 FCC Rcd at 5007-09.

[379] *Id.* ¶ 71, 5 FCC Rcd at 5003.

[380] *Id.* ¶¶ 76, 91, 5 FCC Rcd at 5006, 5111.

138. The language of the 1992 Cable Act clearly indicates that Congress recognized the potential for both beneficial and harmful effects from increased horizontal concentration.[381] In Section 11(c) of the 1992 Act, Congress directed the Commission to establish "reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest."[382] Moreover, Congress required the Commission to consider a number of specific public interest objectives when it established those limits.[383] Those requirements reflect Congressional recognition that there are benefits to increased concentration, including the fact that as compared to smaller system operators, large MSOs can more easily risk providing more diverse, innovative, narrowly targeted, and controversial programming.[384] On the other hand, those requirements also reflect a recognition by Congress of the potential for large MSOs to extract concessions from cable programmers in exchange for carriage of their programming, which could discourage entry of new programming services and adversely impact the diversity of programming available for consumers.[385]

139. Pursuant to Section 11(c) of the 1992 Cable Act, the Commission promulgated horizontal ownership rules.[386] Those rules prohibit any entity from having an "attributable interest"[387] in cable systems that reach more than thirty percent of all homes passed nationwide by cable,[388] or thirty-five percent if the additional systems are "minority-

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[381] *See* H.R. REP. NO. 862, *supra* note 11, at 43 (consolidation has benefited consumers with efficiencies in administration, distribution and procurement of programming, and can promote the introduction of new programming services in the market); S. REP. NO. 92, *supra* note 11, at 33.

[382] Communications Act § 613(f)(1)(A), 47 U.S.C. § 533(f)(1)(A).

[383] *Id.* § 613(f)(2), 47 U.S.C. § 533(f)(2).

[384] H.R. REP. NO. 862, *supra* note 11, at 43; *see also 1990 Cable Report* ¶¶ 82-84, 5 FCC Rcd at 5007-09.

[385] H.R. REP. NO. 862, *supra* note 11, at 42-3.

[386] *Implementation of Sections 11 and 13 of the 1992 Cable Act -- Horizontal & Vertical Ownership Limits, Second Report & Order* ("*Second Ownership Report & Order*"), 8 FCC Rcd 8565 (1993).

[387] In determining what constitutes an "attributable interest," the Commission adopted the broadcast attribution criteria contained in 47 C.F.R. § 73.3555. *See* 47 C.F.R. § § 76.501, 76.503(f). That decision was suggested in Senate Report 92. S. REP. NO. 92, *supra* note 11, at 80.

[388] 47 C.F.R. § 76.503(a).

controlled."[389] In deciding upon those percentages, the Commission stated that it was balancing two Congressional concerns. In particular, the Commission said:

> A 30% horizontal ownership limit is generally appropriate to prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration. Nonetheless, it also ensures that the majority of MSOs continue to expand and benefit from the economies of scale necessary to encourage investment in new video programming services and the deployment of advanced cable technologies."[390]

140. After a federal district court ruled that Section 11(c) of the 1992 Cable Act is unconstitutional,[391] the Commission stayed enforcement of its horizontal ownership rules pending appellate review.[392] In addition, the horizontal ownership rules currently are under reconsideration by the Commission.[393]

1. Status of Concentration in the Cable Industry

141. In most of the local markets where cable operators provide cable service to subscribers, they remain the sole distributors of multichannel video programming. As noted above, there are limited instances of competition through overbuilding in the United States.[394] In addition, suppliers that use technologies other than cable have not yet reached the

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[389] 47 C.F.R. § 76.503(b). "Minority-controlled" is defined as "more than 50 percent owned by one or more members of a minority group." 47 C.F.R. § 76.503(d).

[390] *Second Ownership Report & Order* ¶ 25, 8 FCC Rcd at 8576-77.

[391] *See Daniels Cablevision, Inc. v. United States*, 835 F. Supp. 1, 10 (D.D.C.), *appeal docketed and pending*, Civ. Act. No. 93-5290 (D.C. Cir. 1993).

[392] *Second Ownership Report & Order* ¶ 3, 3 FCC Rcd at 8567.

[393] *See Petition for Reconsideration of Consumer Fed'n. of Am. & Center for Media Educ., Second Ownership Report & Order ("Consumer Fed'n Petition for Recon.")*, MM Docket No. 92-264 (Dec. 15, 1993); *Petition of Bell Atl. for Ltd. Reconsideration, Second Ownership Report & Order ("Bell Atl. Petition for Recon.")*, MM Docket No. 92-264 (Dec. 15, 1993). In their Petition, the Center for Media Education and Consumer Federation of America urge the Commission to establish limits of around 10-20%. *Consumer Fed'n Petition for Recon.* In commenting on that Petition, Viacom recommended a limit of 15%. *Comments on Petition for Reconsideration of Viacom Int'l Inc., Second Ownership Report & Order*, MM Docket No. 92-264 (Feb. 14, 1994).

[394] *Supra* ¶ 54.

subscribership levels necessary for the Commission to conclude that vigorous rivalry currently exists in most local markets for multichannel video distribution.[395]

142. There has been a moderate increase in the nationwide horizontal concentration of the cable industry since the issuance of the *1990 Cable Report*, as measured by the Herfindahl-Hirschman Index ("HHI"),[396] which is a standard measure of horizontal concentration.[397] Whether an HHI measurement, or any measure of concentration at the national level, is meaningful depends on the existence of a national cable market. As is discussed above,[398] the relevant market for the purpose of analyzing competition in the cable industry is generally local, although there may be larger markets in the future, should other technologies become competitive. When examining issues involving cable programming, however, the relevant geographic market may well be national, and in that context, the HHI provides more useful information.

143. In 1990, the national market for the distribution of cable services was unconcentrated, with an HHI of approximately 866. The largest MSO, TCI, had a 24% market share.[399] Taken together, the top four companies had a 47% market share; the top ten had 63%. Between that time and the end of the first quarter of 1994, the market remained "unconcentrated" in terms of horizontal concentration. The HHI for the industry as of March 31, 1994, is 898, which represents a modest increase since 1990.[400] TCI still had the largest market share, 24.8%, an increase of less than one percentage point since 1990. The top four companies still had 47% of the market, and the top ten 63%.

144. At the end of the first quarter of this year, the individual market shares of the rest of the top ten MSOs was as follows: Time Warner was the second largest MSO, with 12.5% of the market; the third largest MSO, Continental, and the fourth largest, Comcast,

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[395] *See infra* § III.B.1.

[396] *See* Appendix G, Tables 1 & 2; NCTA Comments at 20-21.

[397] The HHI is calculated by summing the squares of the firms' percentage shares of the market. 1992 HORIZONTAL MERGER GUIDELINES ¶ 1.5, 4 Trade Reg Rep. (CCH) ¶ 13,104, at 20,573-4 to 20,573-6.

[398] *Supra* ¶¶ 49-53.

[399] Appendix G, Table 2. In 1990, the Commission reported an HHI of 975 (rounding off to the nearest full percentage point). *1990 Cable Report*, Appendix G, Table I, 5 FCC Rcd at 5106-07. All 1990 market share and HHI figures were derived from a base consisting of the top 50 MSOs in the United States. Those top 50 MSOs accounted for 89.6% of the total industry. *Id.* Appendix G, Tables I, II & III, 5 FCC Rcd at 5106-08. In this *Report*, we have revised, and corrected when necessary, the 1990 market share and HHI calculations.

[400] Appendix G, Table 1.

each had approximately 5% of the market; the fifth largest MSO was Cablevision, which had a little less than 4% of the market; the sixth was Cox Cable Communications, Inc. ("Cox"), with a little more than 3%; and the seventh through tenth MSOs each had between 2.25% and 2.5% of the market.

145. By the middle of September, 1994, however, transactions had been announced that would significantly alter the market shares of those top ten companies. Three significant mergers have been announced, all of which are expected to be consummated in the near future:[401] (1) the largest MSO, TCI, has agreed to acquire TeleCable, which would add over 700,000 subscribers to TCI's total, increasing its market share to 26.1%; (2) Comcast has agreed to acquire from Rogers (Rogers Communications) those systems in the United States that Rogers acquired from Maclean Hunter earlier this year, which will give Comcast a 5.6% share and move it from fourth place to third place; and (3) Cox, the sixth largest MSO on March 31, 1994, agreed to acquire Times Mirror Cable Television ("Times Mirror"), which would give Cox a 5.4% share of the market, and make that combined entity the fourth largest MSO, right behind Comcast. In addition to those mergers, Time Warner agreed in September 1994 to (1) consolidate in a joint venture certain of its systems with those operated by Newhouse Broadcasting Corp. and Advanced Publications, Inc., and (2) purchase Summit Communications Corporation (which has 160,000 subscribers). Those transactions will give the second largest MSO, Time Warner, operating control of the seventh largest MSO, causing Time Warner's market share to increase to 15.21%.

146. If the four transactions listed above are consummated, the HHI will rise to approximately 1051.[402] Standard antitrust analysis considers a market with an HHI between 1000 and 1800 to be "moderately concentrated."[403] According to the guidelines developed by antitrust enforcement agencies, "[m]ergers producing an increase in the HHI of more than 100 points in moderately concentrated markets post-merger potentially raise significant

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[401] The management of Adelphia (the 11th largest MSO) has stated that "the telecommunications industry, including the cable television and telephone industries, is in a period of consolidation characterized by mergers, joint ventures . . . ." ADELPHIA COMMUNICATIONS CORP., FORM 10-Q 11 (Jun. 30, 1994). During this period, TCI re-acquired Liberty Media, a transaction approved by the Commission. That acquisition did not change TCI's market share or the HHI measurement relevant herein, as the Commission concluded that throughout the period, the firms were commonly controlled. *See Tele-Communications, Inc. & Liberty Media Corp., Applications for Consent to Transfer Control of Radio Licenses, Order* (*"TCI/Liberty License Transfer Orders"*), DA 94-832 (File Nos. CAR-44064 *et al.* Aug. 1, 1994) (Chief, Cable Services Bureau).

[402] *See* Appendix G, Table 1A.

[403] HORIZONTAL MERGER GUIDELINES ¶ 1.51, 4 Trade Reg. Rep. (CCH) ¶ 13,104 at 20,573-5 to 20,573-6.

competitive concerns depending on [various] factors . . ."[404] None of the four announced mergers would individually increase the HHI by 100 points.

147. When the Commission established limits for horizontal concentration on a national level, it declined to impose regional limits, concluding that "the benefits and efficiencies of regional concentration outweigh any anti-competitive effects in the local programming and advertising marketplace."[405] At this time, the Commission does not have much evidence concerning regional concentration. Bell Atlantic notes that MSOs have been swapping territories with each other, and sees a trend towards large-scale regional concentration of MSOs.[406]

2. *Competitive Effects of Horizontal Concentration*

148. The comments and reply comments that the Commission has received in this proceeding generally reiterate both the benefits and risks of increased horizontal concentration that have previously been described by both Congress and the Commission in the legislative history of the 1992 Cable Act, the *1990 Cable Report,* and in the horizontal ownership rules.[407] One commenter, TCI, provided additional information addressing the issue whether increased horizontal concentration could adversely affect entry of new programming services -- in its view, whether one MSO can accumulate through acquisition a "critical mass" of subscribers to which all programmers must gain access in order to survive or succeed.[408] Such an MSO would be able to dictate terms to programmers, and in effect, dominate the market for cable television programming. TCI, the largest MSO, with approximately twenty-five percent of the nation's subscribers,[409] denied that it had access to

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[404] *Id.*

[405] *Second Ownership Report & Order* ¶¶ 16-17, 8 FCC Rcd at 8573.

[406] Bell Atlantic Comments at 3-4. *See also* GTE Comments at 15. The June 13, 1994 edition of CABLE WORLD reported that Cox Chairman Jim Kennedy indicated that Cox "will focus its acquisition efforts on systems that geographically match the new company's current properties." K.C. Neel, *Cox-Times Mirror Deal Raises Questions,* CABLE WORLD, June 13, 1994, at 1, 60.

[407] *See, e.g.,* Bell Atlantic Comments at 1-4; NCTA Comments at 20; TCI Comments at 12-13, 20-22, App. A at 12, App. B at 7; Time Warner Comments at 6, 33.

[408] TCI Comments, App. B, at 11-14 (Stanley M. Besen, Steven R. Brenner & John R. Woodbury, An Economic Analysis of the FCC's Proposed Cable Ownership Restrictions (Charles River Assocs. Feb. 9, 1993)).

[409] *See* Appendix G, Table 1.

the critical mass of subscribers necessary to make or break a new programming service.[410] Further, it asserted that a large MSO has no rational incentive to restrict its purchases from programmers, or its supply of programming to cable subscribers, by exercising purchasing power over programming suppliers.[411]

149. As shown herein, the persistence of high concentration at the local level tends to impair market performance.[412] In addition, Congress and the Commission have noted that greater national concentration may have both adverse and pro-competitive effects. On the one hand, large MSOs have assisted in the creation and survival of new and underfinanced programmers. On the other hand, those same MSOs may have used their programming purchasing power to deter the entry of new cable programmers or competitive alternatives to cable. To the extent that large MSOs used their power over vertically-integrated programmers to obtain exclusive distribution rights to satellite-delivered programming, and those exclusive rights disadvantaged competitors of those large MSOs, the 1992 Cable Act's program access provisions and the Commission's program access rules appear to have largely addressed the problem.[413]

150. Concentration at the national level enables cable operators to achieve certain efficiencies, such as discounts for programming.[414] Programming costs are a significant portion of total operating costs, accounting for about thirty-six percent of expenditures.[415] Lower prices for programming result from two aspects of firm size. First, given that many programmers grant quantity discounts based on the number of subscribers, larger MSOs will pay lower prices for programs than their non-MSO counterparts. Second, the largest MSOs also may be able to exert superior bargaining power, and thereby, negotiate significant discounts for programming.[416] Lower prices for programming are not, in themselves, a cause

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[410] TCI Comments, App. A at 23. TCI also stated that the point of "critical mass" was different for each type of programming, depending on the cost of production. At another place, TCI acknowledged that increased concentration among MSOs reduces transaction costs for programmers. TCI Comments at 12-13, App. B at 7.

[411] TCI Comments, App. B at 14.

[412] *See infra* § V.A.2.

[413] *See infra* § IV.B.2.a.

[414] TASNEEM CHIPTY, HORIZONTAL INTEGRATION FOR BARGAINING POWER: EVIDENCE FROM THE CABLE TELEVISION INDUS. 3, 20-21 (Conference Paper, AEI Telecommunications Summit: Competition & Strategic Alliances, Am. Enter. Inst., July 7, 1994).

[415] TOWARD COMPETITION, *supra* note 132, at 43.

[416] *Id.* at 3, 20-21. The authors of a 1988 study on concentration contended that discounting was prevalent throughout the cable industry, citing price differentials in excess of

(continued...)

for concern. Discounts on programming can significantly lower the cost of packaging and distributing the cable product. Lower costs also might increase the profits of an MSO which can, in turn, use those funds to increase the supply and quality of programming. However, greater programming discounts, if unfairly and discriminatory granted, may be a competitive concern.

151. Concentration in regional, or locally clustered, marketing areas may also be pro-competitive or anti-competitive.[417] Regional concentration may result in significant efficiencies. A centrally-located regional installation and maintenance office can perform those functions for a number of nearby markets, allowing more efficient use of high-capacity, productive assets. Duplication of other factors of production, such as management, billing, and office space, may also be eliminated by regional clustering. Advertising, marketing and sales functions might realize such economies as well. Larger firms may also realize economies in the purchase of inputs of production, such as programming.[418] Moreover, it may be possible to spread fixed headend costs over a large number of subscribers using fiber optic links. If fiber optic links are substituted for headends, some scale economies could be achieved by eliminating duplication of headend equipment. That flexibility may allow cable firms to adopt more efficient system sizes, and thereby, lower their costs.

152. The sharing of fixed resources required for the deployment of innovative services, including video-on-demand, may also be characteristic of regional economies of scale. Interlinked cable systems will eliminate the need for costly duplication of expensive capital equipment required for these new services. If duplication is required, the access costs related to innovative services may not warrant their provision in less densely populated or rural cable markets. However, if a group of markets were all served from a central location, a standard product could be served to all customers within the cluster. If so, consumers will benefit as the new services will be deployed more rapidly to all markets.

153. Clustering may also reflect the desire of cable operators to enter the telephone business, or it may reflect strategic decisions by cable operators to position themselves to compete against LECs that are poised to enter the market for the distribution of multichannel

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[416](...continued)
90%. NATIONAL TELECOMMUNICATIONS & INFO. ADMIN., U.S. DEP'T OF COMMERCE, NTIA REP. 88-233, VIDEO PROGRAM DIST. & CABLE TELEVISION: CURRENT POLICY ISSUES & RECOMMENDATIONS 81 (1988).

[417] Some of the recently announced mergers involve such clustering. For example, the Cox-Times Mirror transaction involves clusters in Southern California and New England. The Comcast-Maclean Hunter acquisition involves clusters in Michigan, and New Jersey. The Cablevision-Sutton purchase involved a New Jersey cluster.

[418] CHIPTY, *supra* note 414.

video programming.[419] Creating large geographic regions of contiguous cable markets may allow a single MSO to construct more cheaply the network necessary to provide telephone services on a wide scale. By connecting the contiguous systems with fiber optic links, a large regional cable firm may be able to compete better in both voice and video distribution with the RBOCs, which serve large geographic regions.[420] Future cable networks that offer multiple services (voice, video, and data) may require companies to serve larger markets in order to fully take advantage of economies of scale and scope. Therefore, clustering may be viewed as pro-competitive both in terms of cable companies' entry into the market for switched voice and data services, and in terms of positioning themselves for potential competition from LECs in the market for video programming

154. There are, however, competitive risks associated with increased regional clustering of commonly-owned cable systems. The creation of large, contiguous clusters of commonly-owned systems may result in the removal of cable systems that are not affiliated with large MSOs from significant regions of the country. Those "independent" systems may serve presently as a competitive constraint, offering a credible threat of expansion into adjacent markets. If high capital expenditures discourage entry, then adjacent systems may be the most likely entrants, because such systems may be able to use parts of their existing cable plant to support expansion into adjacent areas.[421] The elimination by acquisition of these potential competitors may increase the market power of clustered systems by decreasing the likelihood of entry.

155. A possible consequence of the accumulation of large regional clusters of interconnected cable systems is that such systems may send an entry-deterring signal to potential rivals. When a firm incurs substantial sunk costs by investing in its operations, it signals a long-term commitment to the market. Cable firms making the first move to provide a fiber-based broadband network may dissuade potential entrants from entering the market, or cause then to enter on a smaller scale. For example, a commitment by an MSO to build an integrated broadband network capable of delivering a wide variety of services may discourage the more limited wireless systems from investing in particular markets.[422] Moreover, increased concentration in tightly clustered markets may also enable the few surviving cable operators to coordinate their conduct, with the effect of raising rivals' costs. Nevertheless,

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[419] *See* Geraldine Fabrikant, *Time Warner and Newhouse Form Joint Cable Operation*, NEW YORK TIMES, September 13, 1994, at D1; Paul Farhi, *Time Warner Cable Combination*, WASHINGTON POST, September 13, 1994, at D1; Amy Harmon & J. Lippman, *Times Mirror Deal with Cox Signals New Strategy*, LOS ANGELES TIMES, June 6, 1994, at A1.

[420] *Id.*

[421] *See* C. Cramer, *Local Competition for Telephone Service*, REV. OF INDUS. ORG. 273-91 (June 1994). Existing headends and trunk lines that could be used in expanding the reach of an adjacent cable system account for twenty-five percent of cable plant investment.

[422] *See* JEAN TIROLE, THE THEORY OF INDUSTRIAL ORGANIZATION 368 (1988).

major sunk cost investment by cable systems should expand and improve the quality of services provided to subscribers. Therefore, there may exist complex tradeoffs between the potential consumer benefits that are provided by the sunk cost investments of incumbent cable systems and the potential consumer benefits that new entrants may offer consumers if not deterred by incumbent cable systems.

3. Conclusion

156. The record in this proceeding shows that horizontal concentration in the cable industry has increased moderately since 1990. If the recently announced mergers are consummated, they will result in a further increase in concentration. The Commission will monitor further changes in concentration, and will complete its reconsideration of the horizontal concentration rules. Furthermore, the Commission will continue its analysis of the possible economic efficiencies and inefficiencies of horizontal concentration. Finally, the Commission will continue to evaluate issues associated with industry mergers as required by its implementation of the horizontal ownership provisions of the 1992 Cable Act,[423] as well as by its public interest responsibilities under other provisions of the Communications Act.[424]

B. Vertical Integration in the Cable Industry

157. In the *1990 Cable Report,* the Commission found that vertically-integrated cable operators have the ability to deny competing MVPDs access to programming services in which cable operators have ownership interests.[425] The Commission concluded that such practices could jeopardize the viability of new competition to cable. The Commission also observed that programming services, particularly new ones, at times had difficulty obtaining carriage on cable systems.[426]

158. In response to similar record evidence and in order to promote competition in the program supply and distribution markets, Congress enacted provisions of the 1992 Cable Act that limit the ability of vertically-integrated satellite programming vendors and cable operators to inhibit competitive entry into both the programming supply and distribution

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[423] 47 U.S.C. § 533(f). The Commission's implementation of the horizontal ownership provisions of the 1992 Cable Act will depend on the ultimate disposition of those provisions on appeal, as well as the Commission's reconsideration of its existing horizontal ownership rules, which the Commission has stayed. *See supra* ¶ 140.

[424] *See, e.g.*, 47 U.S.C. §§ 310(d).

[425] *1990 Cable Report* ¶ 113, 5 FCC Rcd at 5021. Vertical integration in the cable industry refers to situations where cable operators, or companies with which they are affiliated, hold interests in vendors that supply video programming to cable systems and other MVPDs, and vice versa.

[426] *1990 Cable Report* ¶ 113, 5 FCC Rcd at 5021.

markets.[427] Specifically, Section 11 of the 1992 Cable Act required the Commission to adopt, *inter alia*, restrictions on the number of channels on a cable system that can be occupied by programming services in which the operator has an attributable interest.[428] Section 12 of the 1992 Act prohibits cable operators and other MVPDs from: (1) requiring that they have a financial interest in a programming service as a condition for carriage; (2) coercing programming vendors to provide exclusive rights as a condition of carriage; and (3) discriminating on the basis of affiliation of vendors in the selection, terms or conditions of carriage.[429] Finally, Section 19 of the 1992 Act prohibits unfair methods of competition and proscribes several specific practices by vertically-integrated satellite cable programming vendors, satellite broadcast cable programming vendors, and cable operators, including, in certain circumstances, the granting of "exclusivity" provisions in cable carriage contracts.[430]

159. On April 1, 1993, the Commission implemented Section 19 by adopting rules that prohibit unfair and discriminatory acts and prohibit or limit the types of exclusive programming contracts that may be entered into between cable operators and vertically-integrated programming vendors (the "program access rules").[431] On September 23, 1993, the Commission issued rules implementing Section 11, which restrict the number of channels on a cable system that may be occupied by programmers affiliated with the owner of that system (the "channel occupancy rules").[432] In a separate order, also issued on September 23,

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[427] Communications Act, §§ 612(f)(1-2), 628, 47 U.S.C. §§ 533(f)(1-2), 548. Congress noted that it had received information that "some vertically integrated MSOs have agreed to carry a programming service only in exchange for an ownership interest in the service. . . . Other witnesses . . . testified that vertical relationships strongly promote diversity and make the creation of innovative, and risky, programming services possible." H.R. REP. NO. 862, *supra* note 11, at 41. The Senate committee stated that "to encourage competition to cable, the bill bars vertically integrated, national and regional cable programmers from unreasonably refusing to deal with any multichannel video distributor . . . ." S. REP NO. 92, *supra* note 11, at 28. Congress also recognized that exclusivity could be a "legitimate business strategy where there is effective competition. Where there is no effective competition, however, exclusive arrangements may tend to establish a barrier to entry and inhibit development of competition in the market." *Id.*

[428] Communications Act § 613(f)(1)(B), 47 U.S.C. § 533(f)(1)(B).

[429] Communications Act § 616, 47 U.S.C. § 536.

[430] Communications Act, §§ 628(b-c), 47 U.S.C. §§ 548(b-c).

[431] *Program Access Report & Order* ¶¶ 123-41, 8 FCC Rcd at 3416-23; *see also* 47 C.F.R. §§ 76.1000 *et seq.*

[432] *Second Ownership Report & Order*, 8 FCC Rcd 8565 (1993), *recon. pending*; 47 C.F.R. §§ 76.501, 76.504. Compliance with those channel occupancy rules is to be monitored in the first instance at the local level and enforced through a complaint process. *Second Ownership Report & Order* ¶¶ 98-99, 8 FCC Rcd at 8606; 47 C.F.R. § 76.504(e).

the Commission adopted rules implementing Section 12 of the Act, which prohibit cable operators from coercing programming vendors into granting them exclusive rights and from discriminating against program suppliers on the basis of the operators' ownership interests (the "program carriage" rules).[433]

160. As discussed in the following sections, the level of vertical integration in the cable industry has remained at roughly the same level as found in the *1990 Cable Report*. However, the program access provisions of the 1992 Act and the Commission's implementation of its program access rules have helped ensure that satellite-delivered programming is made available to competing MVPDs and has reduced the gap between programming prices paid by cable operators and their competitors. Moreover, since 1990, there has also been growth in the diversity and quality of programming services that are offered or whose launch has been announced. Although the Commission believes that its program access rules have generally been successful in ensuring the supply of programming to competing MVPDs, there remain a number of unresolved issues relating to vertical integration that require further attention.

1. Status of Vertical Integration in 1994

161. While the number of vertically-integrated national programming services has grown substantially since 1990, so too has the overall number of programming services available for distribution. Consequently, approximately 53% of programming services are integrated with cable system operators today, compared with 50% of programming services that were vertically integrated in 1990.[434]

162. The Commission noted in the *1990 Cable Report* that all of the successful channels that were introduced after passage of the 1984 Cable Act were affiliated with cable system operators,[435] and today, vertically-integrated national programming services continue to dominate the group of services that are most widely viewed. Twelve of the top fifteen most-watched services, according to prime-time rankings, are vertically integrated, an increase from ten in 1990.[436] Cable operators have interests in fifteen of the top twenty-five

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[433] *Program Carriage Report & Order*, 9 FCC Rcd 2642 (1993).

[434] Since the time of the data used in the *1990 Cable Report*, the overall number of national programming services has increased from 70 to 106. *Compare 1990 Cable Report*, Appendix G, Tables IV-V, 5 FCC Rcd at 5109-10, *with* Appendix G, Tables 3-4 of this *Report*. It appears that MSOs have increased their ownership in national programming services from a total of thirty-five services in 1990 to fifty-six in 1994. *Compare 1990 Cable Report*, Appendix G., Table IV, 5 FCC Rcd at 5109, *with* Appendix G, Table 3 of this *Report*.

[435] *1990 Cable Report* ¶ 80, Appendix G, 5 FCC Rcd at 5007, 5106.

[436] *See* Appendix G, Table 8.

services, an increase from thirteen in 1990.[437] It is too early to determine, however, whether vertically-integrated services that have been introduced since 1990 will be more successful than their non-integrated counterparts.

163. There has been only moderate change since 1990 in cable system ownership of the most popular programming services. All but three of the top twenty-five programming services listed in the *1990 Cable Report* are still in the top twenty-five. One of the three services that have entered the top twenty-five since 1990, Comedy Central, has cable ownership interests, and two, EWTN and Prevue Channel, are not vertically integrated.[438] Since the *1990 Cable Report*, cable operators acquired ownership interests in two of the top twenty-five services and divested interests in one.[439]

164. In total, cable operators have acquired interests in eight existing programming services that had no cable ownership in 1990.[440] Those include the April 1994 acquisition of Paramount Communications, Inc., by Viacom International, Inc., in which Viacom acquired ownership interests in the USA Network and the Sci-Fi Channel.[441] TCI/Liberty Media also acquired a controlling interest in the Home Shopping Network, which offers two programming services.[442] Gaylord Entertainment ("Gaylord"), an owner of three cable systems, acquired Country Music TV, The Nashville Network and superstation KTVT.[443]

165. During this same period, cable operators divested themselves of five existing programming services. Viacom sold its interest in Lifetime to Hearst and Capital Cities/ABC.[444] Cablevision sold its interest in CNBC to NBC.[445] Nostalgia and The Travel

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[437] *See* Appendix G, Table 7. The top 25 programming services are determined by number of subscribers.

[438] *See* Appendix G, Table 7.

[439] Gaylord Entertainment ("Gaylord") acquired The Nashville Network. Viacom acquired the USA Network through its purchase of Paramount and sold its interest in Lifetime.

[440] *Compare 1990 Cable Report*, App. G, at Tbls. 4-5 *with* NCTA Comments, Attachment C, at Tables 1-2.

[441] Viacom Reply Comments at 1-2.

[442] Liberty Media Comments at 12.

[443] *Nashville Network's Parent Going Public*, MULTICHANNEL NEWS, Sept. 2, 1991, at 34; Richard A. Oppel, Jr., *Country and Western Europe; Gaylord Strums Its Stuff Overseas on Cable Network*, DALLAS MORNING NEWS, Mar. 14, 1993, at 1H.

[444] *Viacom Sells 1/3 Interest in Lifetime to Hearst & Capital Cities/ABC for $317.6 Million*, CABLE TV PROGRAMMING, Mar. 31, 1994, at 1.

Channel were reported in 1990 as having MSO ownership, but since then, cable operators have divested those interests.[446] Finally, a few of the programming services listed in the *1990 Cable Report* have gone bankrupt or have merged with other services. The Fashion Channel, a financial investment of TCI, went bankrupt in 1991.[447] In late 1992, VISN, a TCI investment, merged with American Christian TV System ("ACTS") to form the Faith and Values Channel, in which TCI has no ownership interest.[448]

166. Since 1990, thirty-six new programming services have been launched, twenty-two of them since the passage of the 1992 Cable Act.[449] Of the services launched after 1990, twenty are owned in part by one or more cable operators.[450] The Commission has examined the market penetration growth of the fourteen new services that had more than one million subscribers after their launch, the results of which are set forth in Table 4.1.[451]

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[445](...continued)
[445] CABLEVISION SYS. CORP., 1991 ANNUAL REPORT 14 (DEC. 31, 1991).

[446] *Compare 1990 Cable Report*, App. G, tbls IV-V, 5 FCC Rcd at 5109-10, *with* NCTA Comments, Attachment C, Tables 1-2.

[447] TCI Comments, App. A, at 18. QVC, a programming service owned in part by TCI, acquired the bankrupt Fashion Channel's transponder rights and affiliation agreements in 1989. *QVC Buys Out Fashion Channel as Comedy Wars Continue*, COMM. DAILY, Dec. 15, 1989, at 3. In 1991, QVC launched the QVC Fashion Channel. *QVC Will Launch New Shopping Channel*, COMM. DAILY, June 19, 1991, at 6.

[448] *Union of Religious Cable TV Networks Blessed by TCI, Jones*, DENVER BUS. J., Oct. 16, 1992, at 15.

[449] *See* Appendix G, Tables 3-4.

[450] *Id.* However, only 30 of the 98 newly announced programming services are owned, in whole or in part, by cable operators. *See* Appendix G, Table 5.

[451] Of these fourteen new programming services, five -- Fox Net (launched in July 1991), Value Vision (October 1991), Mor Music TV (August 1992), ESPN2 (October 1993) and Americana Television (April 1994) -- had no cable system investment. Cable system operators had investments in nine of the new services examined -- the International Channel (launched in July 1990), Comedy Central (April 1991), Court TV (July 1991), QVC Fashion Channel (December 1991), Cartoon Network (October 1992), Z Music (March 1993), Cable Health Club (October 1993), MTV Latino (October 1993), and the Television Food Network (November 1993). Total United States subscribers taken from *Basic Cable: 1975-1993*, CABLE TELEVISION DEVELOPMENTS 2-A (National Cable Television Assoc. Apr. 1994). Average penetration based on subscriber counts for listed systems as a percent of total United States subscribers. The subscriber counts are taken from *Database, Network Subscriber Counts*, CABLEVISION, Apr. 25, 1994, at 44; *Database, Network Subscriber Counts*, CABLEVISION, Dec. 6, 1993, at 106; *Database, Network Subscriber Counts*, CABLEVISION, (continued...)

Table 4.1
Average Market Penetration of
New Programming Services[452]

	Market Penetration at Launch	*Market Penetration after One Year*	*Market Penetration after Two Years*
Services with Cable Ownership	7.17%	11.11%	20.83%
Services with No Cable Ownership	5.35%	8.66%	7.75%*

* Based on information for only two services.

It appears that vertically- integrated services, on average, achieved greater market penetration in their first two years than services without cable ownership. On the other hand, ESPN2, a new service with no cable ownership had the highest penetration at launch of any new programming services and continues to grow at a steady rate.[453]

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[451](...continued)
Feb. 2, 1993, at 42; *Database, Network Subscriber Counts*, CABLEVISION, Sept. 21, 1992, at 54; *Database, Network Subscriber Counts*, CABLEVISION, May 4, 1992, at 102; *Database, Network Subscriber Counts*, CABLEVISION, Oct. 21, 1991, at 52; *Database, Network Subscriber Counts*, CABLEVISION, Mar. 11, 1991, at 60; *Database, Network Subscriber Counts*, CABLEVISION, Nov. 19, 1990, at 45.

[452] Source for Subscriber Counts: *Database, Network Subscriber Counts*, CABLEVISION, Apr. 25, 1994 at 44; Dec. 6, 1993 at 106; Feb. 2, 1993 at 42; Sep. 21, 1992 at 54; May 4, 1992 at 102; Oct. 21, 1991 at 52; Mar. 11, 1991 at 60; Nov. 19, 1990 at 45. The penetration figures are calculated as the percent of total U.S. subscribers in that year: 1990 -- 54,871,330 subscribers; 1991 -- 55,786,390 subscribers; 1992 -- 57,211,600 subscribers; and 1993 -- 58,834,440 subscribers. NCTA, *Cable Television Developments*, Apr. 1994 at 2-A.

[453] ESPN2 launched with 10 million subscribers, approximately 1.7 million more than Comedy Central's initial 1991 launch, the next-best successful launch of the group studied.

It is unclear to what extent ESPN2's early growth is related to negotiations between its broadcast network corporate affiliate, ABC, and cable system operators relating to the "retransmission consent" provision of the 1992 Cable Act, 47 U.S.C. § 325(b). It has been reported that in those negotiations, ABC tied its consent to the carriage of its broadcast stations by various cable operators to the operators' agreement to carry ESPN2. *See, e.g., American Cable Television; Not Now, Darling*, THE ECONOMIST, Sept. 3, 1994, at 63; Bill Carter, *The Media Business; Networks' New Cable Channels Get a Big Jump on the Competition*, N.Y. TIMES, Mar. 14, 1994, at D7. As discussed *infra* at ¶ 173, NBC and Fox (continued...)

167. Currently, there are fifty-six vertically-integrated programming services.[454] They are owned, in whole or in part, by only twenty MSOs. Twelve of those MSOs have at least a five-percent interest in one or more of the fifty-six services,[455] which qualifies as an "attributable ownership interest" under the Commission's program access rules.[456] An additional eight MSOs hold ownership interests of less than five percent in one or more of those services.[457]

168. Nine of the ten largest MSOs[458] have attributable ownership interests under the program access rules in one or more of these fifty-six programming services.[459] The four largest MSOs have partial ownership interests in seven of the fifteen most popular services and in nine of the top twenty-five.[460] TCI/Liberty Media, the nation's largest MSO, has attributable interests under the program access rules in twenty-three national programming services, which amounts to approximately 22% of the available programming services. Time Warner, the nation's second largest MSO, has attributable interests in sixteen national

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[453](...continued)
have also launched satellite-delivered programming services. As with ESPN2, it has been reported that the NBC and Fox programming services were part of their parents' negotiations under the retransmission consent provision of the 1992 Act. *See* Scott Hettrick, *Putting New Signature on Cable; QVC Tie May Enable CBS to Put Early Failure, Retrans Acrimony in Past*, THE HOLLYWOOD REPORTER, July 1, 1994; Richard Mahler, *A Look at Cable, 1994; Are We Really Close to This?*, L.A. TIMES, Dec. 31, 1993, at F1.

[454] *See* Appendix G, Table 3.

[455] *See* Appendix G, Tables 6, 9-10. The MSOs with attributable interests in programming include Cablevision, Comcast, Continental, Cox, Gaylord, Jones, Lenfest Communications ("Lenfest"), TCI/Liberty Media, Newhouse, Scripps-Howard, Time Warner and Viacom.

[456] *See* 47 C.F.R. § 76.1000(b).

[457] *See* Appendix G, Tables 6, 9-10. Those MSOs are Adelphia, CVI (Cablevision Industries), Colony Communications, C-TEC Cable, Sammons, TeleCable, Times Mirror and TKR.

[458] The only large MSO with no apparent attributable programming interests is CVI. One small MSO, Gaylord, has majority interests in three programming services and operates three cable systems that have a total of 63,195 basic subscribers. Appendix G, Table 9; 1994 FACTBOOK at D-1950.

[459] *See* Appendix G, Tables 6, 9-10.

[460] *See* Appendix G, Tables 7-8.

programming services, or approximately 15% of those available.[461] In contrast, in 1990, TCI held interests in twenty-two national programming services, which was 28.5% of the programming services available at that time. In 1990, Time Warner had interests in eight national programming services, representing 10% of available programming services.[462]

169. Twenty-four of the fifty-six vertically-integrated national programming services are owned, in part, by a single MSO having a 50% or greater ownership interest.[463] Viacom has a 50% or greater interest in twelve services, three of which are ranked among the top fifteen national programming services.[464] TCI/Liberty Media has a 50% or greater interest in three services.[465] Gaylord has a 50% or greater interest in three of the top fifteen national programming services. Four other MSOs have 50% or greater ownership interests in one or two services each.

170. There are nineteen national programming services that are each owned, in part, by several MSOs whose ownership interests, if aggregated, would comprise a majority interest in that programmer. Five of those are among the top fifteen services.[466] In contrast, there are only two vertically-integrated programmers that are each owned, in part, by several MSOs, whose ownership interests, if aggregated, would constitute a minority interest in that programmer.[467] In addition, there are five vertically-integrated programming services that have only one MSO with a minority ownership interest.[468]

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[461] *Id.*, Table 6.

[462] *1990 Cable Report* ¶ 77, 5 FCC Rcd at 5006.

[463] *See* Appendix G, Table 9. The MSOs are Cablevision, Gaylord, Jones, Lenfest, TCI/Liberty Media, Time Warner, and Viacom.

[464] *Id.*

[465] *Id.* TCI also has a 24.8% interest in Turner Broadcasting Systems ("TBS"), and three officers of TCI/Liberty Media are members of the Board of Directors of TBS. TCI Comments, App. A, Chart 4; TBS Comments at 3-4.

[466] *See* Appendix G, Table 10.

[467] *See* Appendix G, Table 10 at 2. One of these, Black Entertainment Television ("BET") was launched without cable investment. However, TCI and Time Warner provided financing to BET in return for equity interests in the programmer. TCI Comments, App. A, at 15-16; Time Warner Comments at 32-33.

[468] *See* Appendix G, Table 10. Only one of those services, The Family Channel, in which TCI/Liberty Media holds a minority interest, is ranked within the top fifteen national programming services. TCI/Liberty Media holds minority interests in the other four services -- Cable Health Club and the three Request Television services. Liberty Media Comments at 9.

171. Also included in the fifty-six vertically-integrated services are the two C-SPAN networks. Those services are considered programming services with cable interests because they receive funding from their cable affiliates. However, according to NCTA, cable operators have no ownership in, or program control over, the C-SPAN services.[469] Finally, there are four national programming services about which NCTA stated that cable system operators had ownership interests, but for which the Commission does not have information regarding the identity of the MSOs that hold the interests, or the amount of those interests in the identified services.

172. To complete the picture of vertical integration in national programming services, the Commission notes that ABC, NBC, and Fox, each own national programming services. ABC holds an eighty-percent ownership interst ESPN and ESPN2, has a fifty-percent interest in Lifetime and has a minority interest in A&E. NBC owns CNBC and America's Talking, has a fifty-percent interest in Bravo and has minority interests in A&E, AMC, and Court TV. Fox owns fX and Fox Net.[470]

2. *Competitive Effects of Vertical Integration*

a. Competitive Access to Programming

173. Commission Enforcement Activities. In contrast to the "substantial evidence of specific problems concerning program access" that were noted in the *1990 Cable Report*,[471] the commenters in this proceeding have not complained about widespread unavailability of programming to distributors competing with cable operators. For example, DirecTV states its belief that the program access provisions in the 1992 Cable Act and the Commission's regulations provide the most effective means for the development of competition to cable.[472] Moreover, the NCTA submits that the program access rules have facilitated increased competition in the video marketplace, and provide more than adequate remedies for instances of unfair conduct by vertically-integrated programming vendors.[473] These comments are consistent with the relatively small number of complaints filed with the Commission concerning denial of access to programming on the grounds of exclusivity agreements.

174. From November 1993, when the program access and carriage agreement regulations took effect, through June 30, 1994, only twelve program access cases were filed;

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[469] NCTA Comments, Attachment C, Table 3.

[470] *Cable Net Ownership*, CABLE TV PROGRAMMING, Aug. 29, 1994, at 2-3.

[471] *1990 Cable Report* ¶ 113, 5 FCC Rcd at 5021.

[472] DirecTV Comments at 2-3.

[473] NCTA Comments at 25-26.

eleven have since been resolved.[474] The Cable Services Bureau has asked for additional information in the one unresolved case. Most of the eleven resolved cases involved exclusivity issues.

175. Another nine cases were filed since late July 1994, and the pleading deadlines in those cases expire in September or October of 1994. Six of those late-July filings involve allegations of price discrimination brought by a single programming distributor. Two of the unresolved matters involve requests by CVI for Sci Fi Channel exclusivity and by Lenfest Communications (fifty-percent owned by TCI/Liberty Media) for exclusivity for a local news service. One additional price discrimination complaint was filed in September. In total, the Commission has received fifteen complaints, five petitions for a finding that exclusivity is in the public interest, and one petition for a waiver of the rules.

176. Two resolved cases involving petitions to the Commission to permit exclusive agreements between vertically-integrated programmers and cable operators are of particular note. In one of those matters, Time Warner filed a petition for exclusivity with regard to the Court TV network. In denying the petition, the Commission first concluded that a party seeking to show that an exclusivity agreement is in the public interest bears the burden of demonstrating that the public interest benefits from exclusivity outweigh its presumptively anticompetitive effects on competing distributors.[475] The Commission then found that continued enforcement of Time Warner's exclusive agreement for the distribution of Court TV adversely affected Liberty Cable's ability to compete effectively in the Manhattan market[476] and would be likely to have similar effects in other markets.[477] The Commission further found that no countervailing public benefits would be derived from the proposed exclusivity. Because Court TV is a viable, successful programming service with a broad and growing national appeal, as shown in part by its thirteen million subscribers, exclusivity was not found to be necessary for survival of the service or to promote diversity in programming.[478] Accordingly, the Commission concluded that continued enforcement of Time Warner's contract with Court TV was not in the public interest.[479]

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[474] A brief description of the resolved cases appears in Appendix F.

[475] *See Time Warner Cable -- Petition for Public Interest Determination Relating to Exclusive Dist. of Courtroom Television, Memorandum Opinion & Order ("Court TV Exclusivity Order")* ¶ 26, FCC 94-132 (No. CSR-4231-P June 1, 1994).

[476] *See Id.* ¶ 37. Liberty Cable is a SMATV system operator that competes in New York City with cable systems owned and operated by Time Warner .

[477] *Id.* ¶¶ 38-39.

[478] *Id.* ¶¶ 43-53.

[479] *Court TV Exclusivity Order* ¶ 55. Following the Commission's decision in this matter, Time Warner withdrew its petition for exclusivity with respect to distribution of

(continued...)

177. In the second case, the Commission found that New England Cable News ("NECN"), a regional news programming source that is fifty-percent owned by Continental Cablevision, had shown that exclusivity was critical to attract investment and secure distribution, which was essential to its financial viability.[480] NECN also showed that exclusive distribution would foster diversity.[481] The Commission found that exclusivity would not have an adverse effect on the development of competition with the cable systems affiliated with it.[482] Therefore, the Commission found that reasonably-tailored exclusivity was in the public interest and granted NECN's petition with certain limits as to the duration of exclusivity.[483]

178. The Commission's enforcement of the program access provisions appears to be meeting one of the goals of Section 19 of the 1992 Cable Act -- ensuring access by competing MVPDs to satellite cable programming from vertically-integrated programming services. There remain, however, several unresolved program access issues, which the Commission considers below.

179. Access to Programming of Non-Vertically-Integrated Vendors. Several commenters, such as WCA, People's Choice, American Telecasting ("ATEL") and Liberty Cable, advocate extension of the statutory prohibitions and requirements to *all* programming vendors -- *regardless* of vertical integration.[484] Those MVPD commenters compete with cable operators and claim to have been denied access to some programming from vendors that are not vertically integrated with cable system operators. Certain MVPDs allege that

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[479](...continued)
Prime Ticket Network. *Time Warner Cable, Petition for Public Interest Determination Under § 76.1002(c)(4) Relating to Exclusive Dist. of Prime Ticket Network, Order*, 9 FCC Rcd 4029 (1994).

[480] *New Eng. Cable News, Petition for Public Interest Determination Under 47 C.F.R. § 76.1002(c)(4) Relating to Exclusive Dist. of New Eng. Cable News, Memorandum Opinion and Order* ("*NECN Exclusivity Order*") ¶ 34-39, FCC 94-133 (No. CSR-4190-P June 1, 1994). The evidence indicated that NECN had about 900,000 subscribers in a potential market of about 3 million.

[481] *Id.* ¶¶ 41-43.

[482] *Id.* ¶¶ 29-32.

[483] Under the terms of the Commission's order, NECN is allowed to offer exclusive distribution rights to cable affiliates for a period of 18 months, but all such exclusive distribution rights must terminate seven years from the effective date of the Commission's order granting NECN's petition. *NECN Exclusivity Order* ¶¶ 49-51, 53.

[484] WCA Comments at 13-14; People's Choice Comments at 5; ATEL Reply Comments at 7; Liberty Cable Reply Comments at 11.

large MSOs exert pressure on non-vertically-integrated programming vendors to provide exclusivity to cable operators in exchange for carriage on their systems.[485]

180. Since these comments were filed, the Commission has amended its program carriage rules to provide standing to MVPDs to file complaints alleging that cable operators have coerced programmers, whether vertically-integrated or not, into granting exclusivity to their competitors.[486] The Commission concluded that coerced programmers might not file complaints because of the potential for damage to their future business relationships with the MSOs that coerced them.[487] The Commission wrote that the mere threat of potential complaints by competing distributors should provide an added check on anticompetitive behavior by MSOs with respect to their negotiation of carriage agreements.[488] The Commission will continue to monitor this situation to determine whether exclusivity agreements granted by services that are not vertically integrated have significant anticompetitive effects.

181. Access to Programming not Delivered by Satellite. Liberty Cable contends that the fact that the program access provisions of the 1992 Cable Act only apply to satellite-delivered programming restricts its ability to obtain attractive, desirable programming that is delivered by other means, and thus impedes its ability to compete with cable competitors who control or otherwise have access to such programming.[489] Liberty Cable further predicts that, unless corrected, this problem will grow in the future because vertically-integrated programming vendors will have the incentive to modify the distribution of their programming, using fiber optics or other non-satellite means, in order to evade application of the program access requirements.[490]

182. Time Warner disputes this concern, stating that satellite transmission remains the most effective method for distributing programming.[491] NCTA argues that the program access provisions were intended to apply to popular, nationally-distributed and satellite-delivered basic and premium services, which arguably are vital to the success of MVPD

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[485] *See* WCA Comments at 13-14; People's Choice Comments at 5.

[486] *Memorandum Opinion & Order* ¶ 40, FCC 94-203, App. A (MM Docket No. 92-265) (released Aug. 5, 1994).

[487] *Id.* ¶ 30.

[488] *Id.* ¶ 24.

[489] *See* Liberty Cable Comments at 13-14.

[490] For instance, Liberty Cable complains that it is unable to secure access to "New York One," a regional news programming service, under the program access rules because it is not "satellite cable programming." *See* Liberty Cable Comments at 13-14.

[491] *See* Time Warner Reply Comments at 23-24.

competitors that use alternative technologies, and were not intended to affect unique, locally-originated programming. NCTA contends that forcing vertically-integrated programmers to provide such programming to competitors of cable system operators affiliated with them would create a strong disincentive to the development of costly and risky ventures like local news programming.[492] The Commission will monitor industry conduct involving programming services that are not delivered via satellite transmission.

183. Alleged Price Discrimination with Respect to HSD Programming Distributors. NRTC and CSS contend that price discrimination continues to be a significant problem for HSD distributors, which allegedly must often pay prices two to five times higher than those charged to comparable cable operators. The programming vendors that filed comments, however, respond that the 1992 Cable Act permits differential pricing with respect to HSD packager-distributors because there are additional costs and services associated with serving such distributors.[493] When it addressed this issue in a prior proceeding, the Commission agreed with the programmers' argument, writing that:

> service to HSD distributors may be more costly than service to others using different delivery systems such as cable operators, as additional costs are often incurred for advertising expenses, copyright fees, customer service, DBS Authorization Center charges and signal security. The record indicates that these cost differences are particularly evident when providing program services to HSD distributors who do not provide a complete distribution path to individual subscribers.[494]

Accordingly, the Commission recognized that pricing differentials with respect to HSD distributors may be justified. The Commission said, however, that it could only determine whether particular cost differentials were justified on a case-by-case basis.[495]

184. In this proceeding, CSS submitted a table showing that the prices charged to HSD distributors for many popular programming services remain significantly higher than listed prices charged to cable operators, with the differentials ranging from 114% to 490%

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[492] NCTA Reply Comments at 10. It is possible, however, that providing locally-originated programming to other MVPDs may prove beneficial to the local cable programmer by spreading the fixed costs of production over a larger subscriber base.

[493] *See, e.g.*, TBS Comments at 2; Superstar Satellite Reply Comments at 6-11; and Southern Satellite Systems ("Southern Satellite") Reply Comments at 3.

[494] *Program Access Order* ¶ 106, 8 FCC Rcd at 3406.

[495] *Id.* ¶ 111, 8 FCC Rcd at 3409-10.

higher for HSD distributors.[496] Other commenters argue that the data in that table are inaccurate, outdated and, in some instances, unverifiable.[497] In its reply comments, HBO stated that counsel for CSS acknowledged in a meeting with HBO's counsel that information in the table was erroneous.[498] The Commission declines to evaluate such data in this proceeding. Rather, such data can best be assessed in the context of individual program access complaints brought pursuant to the Commission's rules.

185. Other Alleged Discrimination Against HSD Packagers. Certain commenters allege that programming vendors discriminate against MVPDs that use specific technologies other than cable through the use of subscriber penetration level requirements, program offering requirements (service must be sold in every package offered by the HSD distributor to a customer), or tier placement requirements associated with lower rates.[499] The only programming vendor to address those contentions in this proceeding was Comedy Partners, which contends that it offers the same rates for high subscriber penetration and overall distribution regardless of the delivery technology used by the distributor.[500] The record is insufficient for the Commission to determine whether discrimination, is in fact, occurring with respect to penetration level requirements, tier placement requirements or service offering requirements. Those issues are best resolved in the context of specific adjudications.

186. Filing of Rate Information. Certain commenters request that the Commission require programming vendors to file rate information with the Commission.[501] In the *Program Access Report & Order*, however, the Commission concluded that a requirement mandating all programming vendors to file rate cards or other rate information would impose an excessive administrative burden on the Commission and would pose difficult questions of confidentiality.[502] The Commission also stated that:

> to the extent that parties have shown that standard "rate cards" generally do not exist, we believe that a filing requirement would impose an excessive constraint on vendors -- thus increasing the possibility of limiting the sale of programming -- and could diminish competitive pricing for multichannel programming through a

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[496] *See* CSS Comments at Appendix A.

[497] *See, e.g.*, Southern Satellite Reply Comments at 2; Viacom Reply Comments at 3; and HBO Reply Comments at 9.

[498] HBO Reply Comments at 9.

[499] *See* CSS Comments at 5; ATEL Reply Comments at 6.

[500] *See* Comedy Partners Reply Comments at 3-4.

[501] DirecTV Comments at 22; GTE Comments at 3; NRTC Comments at 27.

[502] *Program Access Report & Order* ¶ 113, 8 FCC Rcd at 3411.

standardization of higher programming rates as vendors become more aware of the pricing practices by competitors.[503]

b. Commission Rules Promulgated to Assure Diversity in Programming

187. The Commission's channel occupancy rules place a forty-percent limit on the number of channels that a vertically-integrated cable system may devote to video programmers in which the system operator has an attributable interest.[504] In promulgating these rules, the Commission decided to: (1) calculate the forty percent limit from all "activated" channels;[505] (2) measure "attributable interest" in a manner similar to the cable cross-ownership rules;[506] (3) count each channel devoted to vertically-integrated pay and multiplexed services in the forty-percent limitation;[507] (4) exempt local and regional programming from the limit;[508] (5) apply the channel occupancy limits only to the first seventy-five channels of a cable system;[509] and (6) apply the channel occupancy limits even to cable systems subject to "effective competition."[510]

188. While these channel occupancy rules are in effect, the rules are currently under reconsideration by the Commission. Petitioners in the reconsideration proceeding have

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[503] *Id.*

[504] *Second Ownership Report & Order* ¶ 68, 8 FCC Rcd at 8593. A higher limit was set for programming that is minority-controlled. *Id.* ¶ 71, 8 FCC Rcd at 8596.

In addition to channel occupancy regulations, Section 11(c) of the 1992 Cable Act directed the Commission "to consider the necessity and appropriateness of imposing limitations on the degree to which [MVPDs] may engage in creation of video programming." Communications Act § 613(f)(1)(C), 47 U.S.C. § 533(f)(1)(C). The Commission determined that the structural limits imposed by the subscriber limits and channel occupancy rules, as well as behavioral restrictions contained in Sections 12 and 19 of the 1992 Cable Act, already limit the ability of cable operators to impede entry of new programming services, and that additional restrictions on the creation and/or production of video programming were not warranted at that time. *Second Ownership Report & Order* ¶ 106, 8 FCC Rcd at 8608.

[505] *Second Ownership Report & Order* ¶ 54, 8 FCC Rcd at 8588.

[506] *Id.* ¶¶ 61-62, 8 FCC Rcd at 8591-92. These attribution rules, 47 C.F.R. § 76.501, differ from the attribution rules used in the program access context, 47 C.F.R. § 76.1000(b).

[507] *Id.* ¶ 77, 8 FCC Rcd at 8598.

[508] *Id.* ¶ 78, 8 FCC Rcd at 8599.

[509] *Id.* ¶ 84, 8 FCC Rcd at 8601-02.

[510] *Id.* ¶ 88, 8 FCC Rcd at 8603.

requested that the Commission, *inter alia*, lower the 40% channel occupancy limit and change the method by which the limit is calculated.[511] A petition from Bell Atlantic requests that the Commission exempt systems under "effective competition" from the channel occupancy limits.[512]

189. Currently, systems that exceeded the forty-percent limit as of December 4, 1992 are "grandfathered" and those operators are not required to delete attributable video programming services in order to comply with the limit. Instead, the Commission requires that once additional capacity becomes available on such a system (either through system upgrades or programming deletions), the cable operator must fill this additional capacity with video programming from unattributable programming vendors until it is in full compliance with the channel occupancy rules.[513] To enforce the channel occupancy rules, cable system operators are required to maintain records regarding the nature and extent of their attributable interests in and carriage of video programming services, and the Commission welcomes monitoring by local franchise authorities of compliance within their franchise areas.[514]

190. The Commission has not received any complaints alleging violations of its channel occupancy rules or petitions requesting that the restrictions be waived. That silence, ten months after the rules took effect, is a strong indication that there are no significant violations of the rules and that the rules are not unduly restricting the ability of vertically-integrated MSOs to deliver programming to their customers. However, the Commission does not have a sufficient record to determine whether cable systems exclude affiliated programming services because of the rules.[515] Nor is there a sufficient record to address whether the channel occupancy limits have influenced investment of cable MSOs in programming, or whether unaffiliated programming vendors have benefitted from the limits.

3. Conclusions

191. In sum, it appears that the state of vertical integration in the cable industry has not altered significantly since 1990. Cable operators continue to invest in existing and new programming services.

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[511] *Consumer Fed'n Petition for Recon.* (MM Docket No. 92-264).

[512] *Bell Atl. Petition for Recon.* (MM Docket No. 92-264).

[513] *Second Ownership Report & Order* ¶ 93, 8 FCC Rcd at 8604-05.

[514] *Id.* ¶¶ 98-99, 8 FCC Rcd at 8606.

[515] In this regard, the Commission notes that, in 1993, 87% of all cable systems had channel capacities of less than 53 channels, while there are presently 106 national programming services available for carriage. *See* Appendix C, Tables 2-4; Appendix G, Tables 3, 4.

192. The Commission's program access rules and its decisions applying those rules have given competing MVPDs access to programming produced by programmers that are affiliated with cable system operators. The Commission does not find it necessary to make any specific recommendations that Congress amend the program access provisions at this time. Nevertheless, the Commission will continue to monitor the marketplace, and will also rely on MVPDs competing in the marketplace to advise the Commission of further difficulties they encounter in obtaining programming, and the effect of those difficulties on their ability to compete.

193. The Commission has not received sufficient information in this proceeding to enable it to evaluate fully the impact of the vertical ownership rules, and will continue to monitor the impact of those structural limitations.

C. Nature of Technical Changes Affecting Cable Systems

194. As discussed in earlier sections of the *Report,* aspects of industry structure, such as horizontal concentration and vertical integration, might affect competition between cable operators and competing distributors. However, industry structure is not a static concept. Therefore, as historically has been the case in other industries, technological change, whether evolutionary or revolutionary, can directly affect the competitive viability of firms using existing technologies, and has the potential to alter dramatically both industry structure and the overall competitive environment.

195. Telecommunications technologies, including those used in the distribution of video programming, are evolving rapidly. For example, technologies used to transmit voice, video and data are crossing the boundaries that have traditionally separated information distributors. Moreover, the cable industry and competing information distributors are in the midst of deploying new and improved transmission systems, and are projecting the near-term introduction of new and innovative services, that are presently unavailable to consumers, or are only available on an experimental basis. Those changes have the potential to exert a major influence on industry structure, and will affect the sustainability of competition with incumbent cable systems from MVPDs that use technologies other than cable.

196. Developments in system architecture may affect industry structure and the extent of competition.[516] Different distribution media -- copper wire, coaxial cable, optical fiber, terrestrial microwave and satellites -- all differ in their information carrying capacity. Consequently, if technological breakthroughs allow one type of transmission system to increase capacity significantly, that technology may become more advantageous than other technologies. In such a case, the transmission systems using that technology may gain competitive advantages over systems that use other technologies.

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[516] For purposes of this section, system architecture refers to the various media that are used to transmit information, including satellites, terrestrial microwave, optical fiber, coaxial cable and copper, and how those media are used in communications networks.

197. For example, as companies seek to deliver more information, whether it be voice, video or data, through different transmission media, various compression and modulation techniques are used to fit the information within the media, and various switching techniques are used to enhance their ability to deliver the information to end users.[517] Notwithstanding the benefits of increased network capacity, efficiency and functionality that are gained through various modulation, compression, multiplexing and switching techniques, many of these new technologies are designed in such way as to work most efficiently within a particular transmission medium, or with a particular transmission mode. Consequently, architectural design issues are affected by the various methods and technologies used for integrating and transmitting voice, video and data over the same network.

198. However, transmission capacity is not the sole consideration that influences the deployment and utilization of new technologies. Cost may critically influence which technologies win broad consumer acceptance, and which providers thrive in the new communications landscape.[518] The deployment of fiber optic technology is an important example. Fiber optic wiring is often touted for its advantages of high capacity and low maintenance, and it is being widely deployed by cable operators and telephone companies.[519] Cable operators and LECs have both expressed interest in bringing fiber closer to

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[517] *See, e.g., "Building for the Future Video Technology Special, Video Dialtone: Putting the Pieces Together,"* TELEPHONY, July 25, 1994, Special Supplement at 6; *"At Issue: Copper v. Coax,"* TELEPHONY, Mar. 14, 1994, at 18; Paula Bernier, *"Vendors Gear Up for Video Flurry,"* TELEPHONY, June 6, 1994, at 40.

[518] For example, David P. Reed concluded that his study of estimated capital cost functions tentatively demonstrated substantial economies of scope between telephone and distributed video services that are delivered through a hybrid fiber/coaxial cable architecture. DAVID P. REED, THE PROSPECTS FOR COMPETITION IN THE SUBSCRIBER LOOP: THE FIBER-TO-THE-NEIGHBORHOOD APPROACH 12 (FCC Office of Plans and Policy, September 1993). Others conclude that technological developments are increasing the likelihood of local competition. *See, e.g.*, TOWARDS COMPETITION, *supra* note 132, at 42.

[519] Cable operators have been using fiber optics in their system upgrades to replace coaxial trunk lines, as well as to replace the local distribution plant in what is commonly known as "fiber to the neighborhood" or "fiber to the node." The installation of fiber in cable systems has grown from close to zero in 1988, to over 24,000 miles by 1992. CABLE TV TECHNOLOGY, Mar. 19, 1993, at 1. The cable television industry's rate of fiber deployment doubled between 1991 and 1992, and in 1993, over 25% of wired cable subscribers were served by systems employing fiber optics. 1994 Conference on Emerging Technologies ("1994 Conference") 115 (1994) (Society of Cable Television Engineers). It has been estimated that telephone companies had installed over 100,000 miles of fiber by 1992. *Fiber Optics - A New Horizon*, FEDERAL COMMUNICATIONS COMMISSION FACT SHEET, Oct. 1993.

subscribers' homes.[520] Some published reports suggest that the cost of fiber has fallen to the point where it may be economically installed for all but the last mile of network rebuilds and new construction.[521] Others contend that while installation of fiber as part of a hybrid fiber-coaxial architecture is economical, deployment of fiber to the curb or to the home is still prohibitively expensive, and cost considerations associated with how far fiber is deployed into a network may have important competitive consequences.[522]

199. Finally, a number of other interrelated architecture issues exist, which may impact the competitive landscape, including interconnection, consumer interface, and standards.[523] The ability of the public to access, and interact with, the communications networks through modems or converter boxes -- the so-called on- and off-ramps of the national information superhighway -- is an important competitive issue because it visibly manifests the issues of interoperability, interconnectivity and compatibility.[524] The issue of standards, which could impact interoperability, implicates the issue of open versus proprietary architectures.[525] The company (and industry) that captures the lead in these debates may have

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[520] For instance, last year, TCI announced plans to spend $1.9 billion over four years to install 7,000 miles of fiber in at least nine regional hubs. Tele-Communications, Inc. (press release Apr. 12, 1993).

[521] Raymond Smith, COMM. DAILY, Sept. 22, 1989, at 11.

[522] For example, estimates of fiber costs range from $4,000 to $5,000 per fiber mile for HFC architectures and $20,000 per fiber mile for FTTC or FTTH architectures. *See, e.g.*, *"Building for the Future Video Technology Special,"* TELEPHONY, July 25, 1994, Special Supplement, at 13. Leland Johnson suggests that the cost of rebuilding an existing cable system with fiber to the neighborhood is in the range of $250 to $300 per subscriber, whereas upgrading a system with fiber to the curb in order to provide a combination of telephony and video service, increases the cost dramatically to approximately $1,242 per home passed, comparable to the cost of a LEC-provided integrated network of $1,150 per subscriber. TOWARD COMPETITION, *supra* note 132, at 32.

[523] Cable system interconnection is discussed in the Section IV.A of this *Report*.

[524] For example, some observers assert that a coaxial modem connection to personal computers will supplant the coaxial drop to the television as the link into the home. *The Analyst Forum: Communacopia*, GLOBAL RESEARCH (Goldman Sachs, May 19, 1994). Some economists predict that: (1) newly introduced technologies will be biased against compatibility; (2) incentives exist to make converters incompatible and costly unless bundling can occur; and (3) consumer demand for software variety may impact hardware technologies. *Symposium on Compatibility*, 40 J. INDUS. ECON. 1-123 (Richard J. Giblert ed. Mar. 1992).

[525] *See, e.g.*, Lloyd Whittall, III, Architecture-Based Competition and Interoperability in Advanced Cable Systems and the Coming Broadband Local Exchange Infrastructure, (1994) (unpublished graduate thesis, University of Colorado). There currently are about 20 groups.

(continued...)

a significant competitive advantage over other information providers. Such an advantage could potentially be extended into competitive advantages in other areas where interoperability and compatibility are desired.

200. The foregoing discussion suggests that it is too soon to draw any conclusions regarding the ongoing dynamics of technological change that permeate the telecommunications industry today. Nevertheless, significant issues that may have a dramatic effect on how competition develops in the delivered multichannel video programming industry are coming into focus. The Commission's ongoing review of such issues will be essential to the formulation of public policies for video distribution markets that will provide consumers with early access to the remarkable advantages that such technologies seem to promise.

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[525](...continued)
working on, and competing to have their particular approach adopted as, the international digital industry standard.

V.
STATUS OF COMPETITION IN THE MARKET FOR THE DELIVERY OF VIDEO PROGRAMMING

A. Extent of Competition and Assessment of Market Performance

1. Overview

201. The Commission finds in this *Report* that cable television remains the dominant medium for providing consumers with multichannel video programming. Most local markets for the distribution of multichannel video programming are highly concentrated, and for most consumers, cable television is the only provider of multichannel video programming. There are presently only a few scattered areas of the country where the local cable operator faces direct competition from an overbuilder.[526] Moreover, providers using alternative technologies have not yet reached the subscribership levels necessary for the Commission to find the existence of vigorous rivalry in the market for multichannel video distribution. Relative subscriber levels for the cable industry and competing distribution technologies, to the extent available, are shown in Table 5.1 below.

TABLE 5.1
Estimated Subscribership of Various
Video Programming Distribution Systems (in millions)

SYSTEM	*1990*	*1991*	*1992*	*1993*	*CURRENT*
CABLE (mil)	51.7	53.4	55.2	57.4	57.9
HSD	.7	.8	1.0	1.6	2.0
MMDS	.3	.2	.3	.4	.5
SMATV					1.0
OVERBUILD			1.3		n/a
PRIMESTAR					.1
DIRECTV/					n/a
VDT					none
LMDS					n/a

n/a = not available. Shares for alternative distribution technologies include areas not passed by cable.[527]

[526] *See supra* Section III.B.

[527] Sources for the figures in Table 5.1 are as follows: **CABLE** - *History of Cable & Pay TV Subscribers & Revenues*, CABLE TV INVESTOR, March 31, 1994, at 9. **HSD** --

(continued...)

202. The dominance of cable television in local markets may be enhanced by horizontal concentration of cable MSOs nationwide. This *Report* finds that horizontal concentration among the largest cable MSOs has increased only modestly since the time of the *1990 Cable Report*. The Commission notes, however, that there have been several proposed transactions in 1994, most notably, TCI-TeleCable, Cox-Times Mirror, Comcast-Maclean Hunter, and Time Warner-Newhouse, that will, if consumated, involve the largest MSOs acquiring control over a number of additional cable systems. In addition, MSOs appear to be creating regional "clusters" of cable systems and franchises. If those trends persist, the cable television industry will become increasingly concentrated nationally and regionally over the next few years.[528] In addition, MSOs continue to invest in video programming vendors. The Commission anticipates that such investment will continue, and that the Commission's program access and carriage rules remain necessary to prevent the potential abuses of such investment.[529]

203. In the longer term, increased rivalry in the market for delivered multichannel video programming should result in lower prices relative to present cable rates, and in a

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[527](...continued)
1990-91, 1992, and 1994 net authorizations supplied by letter received by telecopier on September 8, 1994 from Brigette Engel, of General Instrument, Inc. to Cable Services Bureau Staff, and General Instrument Press Release (Aug. 18, 1994); 1993 net authorizations from *GI Net Authorization Near 1,900,000*, SKYREPORT, July 1994 at 5. HSD subscribership estimate may also include HSD subscribers that subscribe to cable service; **MMDS** -- 1990 and 1994 from WCA Comments at 2, n.3; 1991 & 1993 from *Average Annual Subs*, WIRELESS CABLE INVESTOR, June 30, 1994, at 1; average annual subscribers for 1992 from telephone interview with Paul Kagan Associates, Inc. personnel explaining details of WIRELESS CABLE INVESTOR, June 30, 1994 at 1; **SMATV** -- from *Cable & Pay TV Census -- August*, MARKETING NEW MEDIA, Aug, 15, 1994; **OVERBUILD** -- 1992 from *P.K. Cable TV Overbuild Census*, CABLE TV FRANCHISING, Apr. 30, 1992, at 4; The Commission has been unable to update 1992 estimate, and will attempt to ascertain subscribership levels of overbuilt systems in future reports; **PRIMESTAR** -- Tom Kerver, *DBS: One Plus One Equals Three*, CABLEVISION, May 23, 1994, at 82; **DIRECTV/USSB** -- roll-out of DBS services in selected markets began on June 17, 1994, and accordingly, meaningful subscription figures are not yet available; **VDT** -- permanent VDT service is not presently available, although the Commission has recently granted application of Bell Atlantic to provide permanent service in Dover, New Jersey; **LMDS** -- the Commission does not possess sufficient information to estimate the number of households that subscribe to the services of LMDS programming providers, but the number of subscribers appears to be *de minimis*.

[528] *See supra* Section IV.A.

[529] *See supra* Section IV.B.

substantially broadened array of programming options for increasingly specialized audiences.[530] In addition, consumers should receive more pricing options. Such rivalry may also be expected to provide a stimulus to more rapid development of new technologies and product innovation. At present, market performance in local cable markets does not yet reflect the benefits of this competitive rivalry. Therefore, lowering barriers to entry is likely to lead to significant gains in consumer welfare.

2. *Market Performance Indicators*

204. The effectiveness of the existing level of competition at improving *market performance, i.e.*, the extent to which a given market satisfies consumer demand in the least costly manner, may be assessed using several *market performance indicators*. Among various alternative indicators of market performance, emphasis is placed on measures that provide insight concerning the current relationship of cable rates to the cost of production.[531] Empirical measures of market power provide such insight, and are discussed in the following paragraphs and Appendix H. Other indicators of market performance, such as the price effects of overbuild competition and improvements in cable services, are also considered.

a. Pricing Above Competitive Levels Indicates Market Power

205. The following discussion emphasizes on two key indicators that suggest that cable systems are currently exercising market power: (1) the *q ratio*, a ratio of the market value of cable assets to the replacement cost of such assets; and (2) pricing analyses showing that prices in monopolized cable distribution markets exceed those in similar cable markets where there exist cable system competitors. If a firm can set its prices *above* its costs and earn excess economic profits for a sustained period of time, then the firm possesses *market power*.[532]

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[530] As more fully discussed in Appendix H, it is also possible that competition in some local cable markets might tend to emphasize rivalry between and among highly-differentiated program packages, rather than price competition for broadly similiar program packages offered by competing video programming suppliers.

[531] No direct evidence is presented in this *Report* concerning the cost of producing basic cable services provided by local cable systems. As shown in Appendix H, *indirect* methods are used to infer the magnitude of the relationship between basic cable rates and the marginal cost of production.

[532] Market power sustained over a substantial period of time often signals the existence of some impediment to market entry, although the impediment need not constitute a *policy-relevant barrier to entry*. A policy-relevant barrier to entry (1) is any cost that a potential entrant must incur in the course of market entry that an incumbent firm need not incur, and (2) implies a net loss in consumer welfare if the barrier persists. *See* Appendix H.

206. In the past, the Commission has looked to the q ratio[533] as an indicator of market power.[534] Under conditions of perfect competition, potential buyers of the assets of a competitive firm which, by definition, does not earn excess economic profits, are unwilling to pay much more than the reproduction cost of the firm's tangible assets. As a result, the market value of a firm selling in markets that approximate the conditions of perfect competition is roughly equal to the reproduction cost of the firm's tangible assets. Given this logic, the q ratio of a firm supplying competitive markets and earning no excess economic profits over the longer term should equal one, *i.e.*, the market value of a firm's assets should equal their replacement value.

207. Alternatively, q ratios well in excess of one suggest that a firm, or a collection of firms in an industry, may be earning excess profits. Such a result is consistent with the presence and exercise of market power, inasmuch as excess profits are generated by price-cost margins that are greater than what may be required simply to recover the total cost of production in the presence of economies of scale.[535] If a q ratio is greater than one, then another firm would find it profitable to enter the market. Such entry would increase market supply, force prices and profits down towards a competitive level, and hence, reduce the market value of the incumbent firm or firms. When the q ratio reached one, entry would no longer be profitable.

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[533] The q ratio is subject to some theoretical limitations. *See infra* note 541. For a more thorough analysis of the q ratio from an industrial organization perspective, *see* Eric Lindenberg & Stephen Ross, *Tobin's q Ratio and Industrial Organization*, 54 J. BUS. 1-32 (Jan. 1981); Michael Smirlock, Thomas Gilligan & William Marshal, *Tobin's q and the Structure-Performance Relationship*, 74 AM. ECON. REV. 1051-60 (Dec. 1984). *See also* Appendix H (theoretical discussion of q ratios); *1990 Cable Report* ¶¶ 54-90, App. E, 5 FCC Rcd at 4997-5011, 5071 (contains a more detailed discussion of the q ratio).

[534] *See 1990 Cable Report* ¶¶ 55-59, 5 FCC Rcd at 4997-99. An alternative measure of market power is the *Lerner Index*, which is defined as the percentage difference between price and the marginal cost of production at the profit-maximizing level of production. As reported in Appendix H, the estimated Lerner Indices suggest that current cable industry prices substantially exceed marginal costs. The prevalence over time of prices in excess of marginal costs often indicates the existence of market power. However, if the technology of production implies substantial fixed costs and economies of scale, prices above marginal costs may *not* provide conclusive evidence of market power. As is shown in Appendix H, there exist both non-trivial fixed costs and economies of scale (albeit limited) in the cable industry. As explained in Appendix H, such cost characteristics complicate the interpretation of Lerner Indicies as measures of market power. Consequently, the Commission does not place primary reliance on the Lerner Indices in this *Report*.

[535] The definition of economies of scale and emperical estimates of such economies in the cable industry are provided in Appendix H.

208. Professor Paul MacAvoy, currently Dean of the School of Organization and Management at Yale University, submitted q ratio estimates in connection with the *1990 Cable Report*. His "best estimate" of the q ratio for the cable industry was 4.3 for September 30, 1989.[536] In connection with this *Report*, the Commission calculated some q ratios based on more recent data. The calculations are useful not only because they provide some indication of the current level of market power in the cable industry, but also because, with some qualifications, they permit a comparison of the market power levels in 1989 with those of more recent times.

209. There are two primary techniques for calculating market value, both of which were used by the Commission in the q ratio calculations that were prepared for this *Report*. One, which MacAvoy refers to as "public" market value, involves the calculation of the sum of a firm's liabilities and the value of its outstanding stock.[537] In order to utilize this technique, it is necessary to have a sample of firms that are involved only in cable television delivery. MacAvoy identified five such firms for 1989. The Commission was able to identify four such firms for 1993, only two of which are also in the MacAvoy sample. The second technique, which MacAvoy labels "private" market value, involves the calculation of the average (weighted by number of subscribers) of per subscriber selling prices of cable companies.[538] In this second method, only cash transactions are included, because it is difficult to determine market values for transactions that include non-cash components.[539]

210. There are also two primary techniques for calculating replacement costs. One is based solely on financial data, and consists of an estimate of the adjusted book value of tangible assets ("net plant"). The figure for net plant is adjusted for inflation, and then added to other tangible assets. The second method uses other tangible assets from financial accounts, but substitutes a construction cost estimate for net plant. The estimated cost of new construction per subscriber is depreciated by the average age of cable plant, and other tangible assets are added to calculate replacement cost. Once again, the financial data must come from firms that are involved only in cable television delivery. Because the bulk of tangible assets tend to be accounted for by net plant, the financial data play a smaller role in estimates that utilize construction costs. In calculating q ratios based on replacement costs that are estimated from construction costs per subscriber, MacAvoy chose the median of several construction cost estimates.[540]

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[536] *1990 Cable Report* ¶ 57, 5 FCC Rcd at 4998 (*citing* USTA Comments, App. 5, *1990 Cable Report*, MM Docket No. 89-600).

[537] USTA Comments, App. 5, *1990 Cable Report*, 5 FCC Rcd 4962 (MM Docket No. 89-600).

[538] *Id.*

[539] For details of the Commission's q ratio calculations, see Appendix I.

[540] *See* Appendix I.

211. The following table presents five q ratio calculations based on current data, and also sets forth the MacAvoy calculations to which they are most comparable. As explained in Appendix I, none of the current calculations are perfectly comparable to the MacAvoy calculations. However, the comparisons are at least suggestive of possible trends in cable market power. Appendix I contains a more detailed discussion of these calculations.

TABLE 5.2:
Estimated q Ratios for the Cable Industry

Method	*Current q Estimates*	*MacAvoy 1989 q Estimates*
Public Market Value/Adjusted Book Value (Current, four firms; MacAvoy five firms)	4.47	4.30
Public Market Value/Adjusted Book Value (for two firms common to both samples)	4.52	4.17
Public Market Value/Median Construction Cost (Current, four firms; MacAvoy five firms)	5.23	4.56
Private Market Value (1993 transactions)/Median Construction Cost	4.11	6.2
Private Market Value (some 1994 transactions)/Median Construction Cost	3.95	6.2

Source: *See* Appendix I.

212. Even with the caveats enumerated in Appendix I, the current q ratios suggest that, overall, cable television operators possess substantial market power. The comparisons between 1989 and 1993/94 are inconclusive, however, allowing both the inference that market power may be increasing, based on the calculation that uses public market values, and the inference that market power may be decreasing, which is derived from the private market value calculation.[541]

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[541] As a measure of market power, the q ratio must be carefully interpreted. As noted in the *1990 Cable Report,* the q ratio is subject to some limitations. Accordingly, a conservative interpretation of a q ratio views it as an upper bound indicator of monopoly power, since it may also reflect monopsony power possessed by the firm or industry. *1990 Cable Report* ¶ 59, 5 FCC Rcd at 4999. Additionally, q ratios may also reflect certain financial risks unique to the industry or the ownership of a scarce resource that may not be generally available to competitors. Moreover, q ratios greater than one might indicate a current disequilibrium between market demand and supply as a consequence of sustained growth in demand over time. *See 1990 Cable Report*, App. E, 5 FCC Rcd at 5071-82.

(continued...)

213. Price Effects Shown by Overbuild Competition and the Commission's "Competitive Price Differential." The Commission received significantly more reliable pricing information in this proceeding than was available at the time of the *1990 Cable Report*. The exercise of market power (pricing well in excess of marginal cost) in local markets is shown by (1) evidence concerning price changes in local cable markets following the entry of second cable companies, and (2) the Commission's cable rate reregulation orders, in which it estimated a "competitive price differential" by focusing primarily on the difference between prices charged by monopoly cable systems and those facing direct competition.

214. A number of empirical studies have addressed the effects of two-firm (duopoly) competition in cable television markets using published or survey data.[542] The focus of those studies has been primarily on how such rivalry affects prices. A simple test for the presence of competitive price effects is to compare prices in monopoly and duopoly cable markets. Those studies consistently show that prices in duopoly markets are *significantly lower* than in monopoly markets. For example, in a 1987 survey, the price of a package including basic service plus one premium service was found to be 23.5% lower in competitive cable markets than in monopolized markets.[543] More recently, a 1992 study found that basic rates were 21.9% lower in competitive markets than in monopolized markets.[544]

215. While studies using survey data show significant price differentials in duopoly cable markets, the survey approach fails to take into account the effects of local cost and demand conditions. For example, no consideration is given to *per capita* income in the cable market. If cable demand is sensitive to income levels, then ignoring that effect "biases" the estimate of the price effect of competition. Furthermore, the survey method fails to account for the number of available channels, the cable system size, regional wage rates, and other factors that are important determinants of the supply and demand for cable service.

216. An improved estimate of the effects of entry can be produced by using a methodology that accounts for demand and cost differences across markets. A number of

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[541](...continued)
Given such possible qualifications, a q ratio only slightly greater than one need not necessarily represent conclusive evidence of market power. The magnitude of the estimated q ratios reported in the table above, however, suggests the presence of substantial market power, notwithstanding the possibility that the estimation methodology may be subject to the limitations that the Commission recognized in the *1990 Cable Report*. For further discussion of qualifications in the interpretation of q rations, see Appendix H.

[542] *See also supra* Section III.B.

[543] See Thomas W. Hazlett, *Cabling America: Economic Forces in a Political World*, FREEDOM IN BROADCASTING 208-23 (C. Veljanovski ed. 1989).

[544] *See PK Overbuild Census, supra* note 527, at 4.

empirical studies have employed econometric techniques to estimate a competitive differential that is adjusted for demand and cost factors. Those studies support the findings of the more simple survey approach, and find cable rates in competitive markets to be significantly lower than rates in monopolized cable markets, even when other factors are held constant. For example, adjusting for a number of factors such as system size and the number and type of channels available, Stanford Levin and John Meisel found that cable rates are, on average, $3.33 lower in competitive cable markets than in monopolized markets.[545] In a far more sophisticated study, Richard Beil, *et al.* estimated a competitive differential of $3.85, other things remaining constant, which amounts to a savings of over twnety percent for basic cable service.[546] That study also found that systems in competitive markets priced premium services $1.10 lower than did monopoly systems.

217. A few recent studies, including the Commission's re-calculation of the competitive differential for the purpose of rate regulation, have improved the measure of competitive price used in their statistical models to account for differences in the extent of competition across competitive cable markets. Those studies measure competition as the *degree of overlap* between competing systems. The application of this measure carries with it the assumption that competitive prices in cable markets *can* vary depending on whether the overbuilder competes over the entire market or only overlaps with the incumbent in part of the market.

218. When it re-calculated the competitive differential, the Commission adopted an overlap measure of competition, where competition is measured by the percent of the franchise market that both rivals serve. Adjusting for a number of variables including firm size, the number of available channels, and income, the Commission's analysis estimated a sixteen percent competitive differential, *i.e.,* that prices in areas served by two cable systems were sixteen-percent lower than prices in monopolized areas.[547] That differential, along with the differentials for other systems subject to effective competition as defined in the 1992 Cable Act, formed the basis for the rate rollback in the *1994 Rate Report & Order*.[548] Using the same measure of competition, a recent econometric study not only adjusted for demand and cost differences, but also accounted for other possible biases that might distort empirical estimates of the price difference between monopoly and duopoly cable distribution markets.[549] That study produced the estimate that a completely overbuilt system will have rates approximately twenty-percent lower than a monopoly cable system, holding other things constant. The study allowed for demand elasticity estimates for both monopoly cable systems

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[545] *See* Levin & Meisel, *supra* note 130, at 519-528.

[546] *See* Beil, Dazzio, Ekelund & Jackson, *supra*, note 130, at 401-15.

[547] *1994 Rate Report & Order*, ¶ 97 (MM Docket No. 92-266).

[548] *Id.* ¶¶ 25-33.

[549] *See* Ford, *supra* note 130.

and systems in duopoly markets. The demand curve for firms facing direct competition was found to be *more elastic* than the monopolist's demand curve, implying that a cable system's market power is constrained by overbuild competition.

219. Excess Profits as an Inducement for Competitive Entry. New firms are likely to enter an industry if current and anticipated profits are supracompetitive. Large investments by competitors using alternative technologies, such as MMDS and DBS, and the history of attempted entry by overbuilding,[550] suggest that potential profits in the cable market are substantial, a perception that is consistent with the foregoing discussion of pricing in local cable markets. The proposed entry into video distribution by local telephone companies is also noteworthy, since the high cost of upgrading telephone networks in order to allow video distribution might not be justified if LECs did not believe that there was potential profit in video packaging and distribution. There may be other explanations for the interest in competing with the cable operators. The prospective entrants may believe that they can provide services at lower costs than the incumbents, or they may believe that the market demand for additional services that can be supplied with cable programming is large enough to support additional entry. Therefore, while interest in entry in this market may suggest that prices exceed costs, such evidence taken alone is not conclusive with respect to the potential profitability of additional entry in local cable markets.

b. Other Indicia of Market Performance

220. The finding of an exercise of substantial market power in local markets implies a loss of economic efficiency.[551] Market performance and consumer welfare are adversely affected by such losses. Other data suggest, however, that to some extent cable operators may be responding to consumer preferences and the resulting growth in demand for video programming. In this proceeding, the Commission has found that the demand for the multichannel programming services provided by local cable systems has continued to grow since 1990. The cable industry has responded positively to this growth in demand by

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[550] Although overbuild competition today is limited, it is difficult at present to reach definitive conclusions about the profitability of direct competition with incumbent cable systems. Any analysis of competitive market entry must account for the effects of the local franchising process that may block, delay, or otherwise discourage competitive entry, notwithstanding the prohibition of such behavior by the 1992 Cable Act.

[551] Economic efficiency in the consumption of goods or services, or in their production, is achieved if it is impossible to improve the economic welfare of at least one individual without simultaneously making some other person worse off as a result of a change in the existing allocation of resources. In general, output prices equal to the marginal cost of production result in an economically-efficient allocation of resources. The exercise of market power results in output prices that exceed the marginal cost of production. As a result, consumers purchase less output than they would if output price were equal to the marginal cost of production. The value of such foregone consumption is a measure of economic inefficiency, and represents a loss in consumer welfare.

increasing the number of homes that could receive cable service ("homes passed") to 92.9 million in 1993, an increase of 8% over the number of homes passed in 1990. Actual demand for cable services grew from 51.7 million households in 1990 to 57.4 million households in 1993. Accordingly, nearly 60% of all television households in the United States subscribed to cable services in 1993, up from 55.4% in 1990. Moreover, mean cable penetration (the fraction of households with access to cable services that actually subscribe) increased from 60.1% to 61.8% from 1990 to 1993.[552]

221. Broad consumer acceptance of the video programming services offered by cable systems is reflected in the growth in cable industry revenues from $17.86 billion in 1990 to $22.94 billion in 1993. That growth in revenues represents a greater than 28% increase from 1990 through 1993. As is more fully discussed above in section II, such revenue growth clearly suggests that consumers find the growing array of programming services offered by cable systems responsive to their preferences for such programming services.

222. Clearly, the cable industry continues to respond positively to the overall growth in consumer demand for more services and improved programming choices. Yet, growth in output has been accompanied by non-competitive pricing of services that may have suppressed subscribership, relative to that which would otherwise prevail if basic service rates were lower. As shown in Appendix H, the demand for basic cable service tends to be responsive to reductions in price (*i.e.*, demand is price elastic) at currently observed price levels. Therefore, price reductions would be expected to stimulate an increase in penetration levels while improving the net benefits that consumers derive from cable services. Accordingly, there remain today substantial opportunities for improving consumer welfare.

223. Other indicators of economic efficiency as a criterion of market performance include measures of technological change in production, product innovation, and industry expenditures on research and development. Unfortunately, useful data on such indicators of economic efficiency in the cable industry are limited. As a result, the Commission does not possess sufficient data for a complete empirical assessment of whether the cable industry is performing well by enhancing consumer welfare. Nevertheless, evidence developed in this *Report* facilitates a qualitative assessment of these indicators of industry performance.

224. Although difficult to measure and assess at present, the quality of multichannel video programming services offered by cable systems appears to have improved since 1990, when measured in terms of the number of channels available to subscribers. The record in this proceeding demonstrates that cable systems with the capacity for providing thirty or more channels accounted for over 77% of all cable systems for which information was available in 1993.[553] That percentage represents an increase from 67% in 1990. Growth in the number of programming networks is another rough indicator of improvements in the quality of cable

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[552] *See supra* Section II.

[553] *Id.*

service. The record reveals that the total number of networks increased by over 51% from 70 in 1990, to 106 at present. Those improvements in service quality should permit a closer alignment between diverse consumer tastes for video programming and the ability of cable systems to meet such consumer demand. Improved matching of consumer demand with the available supply of video programming through time represents an improvement in economic efficiency.

225. Industry investment expenditures represent a commitment by firms to meet current and future growth in consumer demand while improving both product quality and variety. Investment spending is the vehicle, therefore, for implementing improvements in the technologies of production, and for implementing product or service innovations. The record before the Commission shows that total cable industry capital investment has fluctuated around $3 billion annually since 1990, but is projected to increase to $3.8 billion in 1994.[554] Such spending reflects a commitment to implement technical change that will increase the quantity and improve the quality of cable service in the future.

226. As described in Section IV.C, *supra*, the ongoing installation of fiber optic distribution facilities in local cable systems will dramatically increase transmission capacity while expanding the number of services that cable systems may eventually offer their subscribers. Moreover, the cable industry supports a substantial research and development program through Cable Labs. That industry research effort may well result in a new cable network structure incorporating technical changes that will improve the quality and variety of services offered to subscribers over the longer term.

c. Conclusion

227. Current market performance in the multichannel video programming distribution industry, when assessed in terms of several indicators of economic efficiency, is mixed. While the industry is responsive to growth in consumer demand, the output is supplied to consumers at prices that often imply substantial losses in economic efficiency. The industry continues to invest in the deployment of improved video distribution facilities, which should offer the consumer expanded video programming options. The industry also invests in research and development, which should improve the capabilities and performance of local cable networks and services in the future. The willingness of new entrants to invest substantial resources in competition with the incumbent cable systems suggests, however, that there exist further opportunities for improved market performance.

3. Existing and Potential Impediments to Competition

228. In this Section of the *Report*, the Commission addresses certain existing and potential impediments to competitive entry that may have a dampening effect on the extent of competition in the video programming delivery market. In particular, the *Report* addresses impediments flowing from the strategic behavior of incumbent firms, legal restrictions, and

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[554] *Id.*

technological bottlenecks. As will be discussed, in certain instances, those impediments may block potential entrants from entering the market altogether. More commonly, however, the impediments serve to increase the cost of a rival's entry, and hence its cost of production as compared with that of incumbent firms.

a. Strategic Behavior to Deter Competitive Entry

229. The cost of constructing a cable distribution network may be viewed as a sunk cost, *i.e.*, an operator's investment in its cable plant cannot typically be physically redeployed to some other profitable use if operation of the system were to become unprofitable.[555] The existence of those sunk costs creates strong incentives for the incumbent cable operator to engage in strategic behavior designed to protect that investment. While such behavior may take the form of vigorous competition, which enhances consumer welfare, cable operators also have the incentive to engage in strategic behavior designed to deter entry by potential rivals.

230. Access to Program Supply. Under certain conditions, agreements that restrict a supplier's right to deal with competitors of a dominant downstream firm can have the effects of raising its rivals' costs by restraining the availability of needed inputs and of decreasing the demand for programming. Through such exclusionary rights agreements, a dominant firm can deter competitive entry, and retain the power to raise prices in its output market.[556]

231. One example of such behavior in the cable industry involves efforts by cable operators to restrict the supply of programming to suppliers that use alternative distribution technologies. As Congress recognized in enacting the program access provisions of the 1992 Cable Act, by controlling access to programming supply, cable operators were able to inhibit competitive entry and maintain their monopolies over the distribution of programming in most markets.[557] In this proceeding, the Commission has found that following the implementation of the program access provisions of the 1992 Act, the cable industry's use of program availability as a means of deterring entry has, to a large extent, abated. The record also reflects a number of continuing concerns over potential strategic behavior by cable operators

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[555] The concept and economic significance of sunk costs are discussed in Appendix H.

[556] *See* Tom Krattenmaker & Steve Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power Over Price,* 96 YALE L. J. 209, 223-224 (1986). As recognized by Congress in the 1992 Cable Act, and discussed in Section IV, *supra*, exclusive contracts may not be inefficient or anticompetitive if the video programming and local distribution markets are sufficiently competitive.

[557] *See Court TV Exclusivity Order* (No. CSR-4231-P)

involving access to programming that are not within the purview of the current regulatory scheme.[558]

232. In particular, the program access provisions of the statute only apply to "satellite cable programming." Therefore, as discussed above, programming services distributed by any other means are not subject to the program access requirements.[559] As a result, some commenters raise the possibility that cable operators may have the incentive and ability to engage in strategic behavior designed to shift programming from satellite distribution to fiber optic or some other form of terrestrial distribution, thereby removing the programming from the purview of the program access provisions. In addition, regional clustering of systems combined with a system's ownership of one or more regional programming networks, may create additional incentives for the operator to engage in strategies designed to deny competing distributors access to its programming. One such strategy could include shifting regional programming to terrestrial distribution to facilitate denial of the programming to competitors.

233. A second area in which commenters argue that cable operators may have the continued ability to engage in strategic behavior with respect to program access matters involves the program access provision's limitation to programming supplied by vertically-integrated programming vendors, *i.e*, vendors in which cable operators have an attributable interest.[560] Thus, commenters have suggested that cable operators, using their buying power over programmers, can extract concessions from non-vertically integrated programmers that raise rival operators' costs of obtaining programming or deny them access to programming altogether. Moreover, as the industry becomes further concentrated, the potential for collusion among operators jointly to pressure programmers to adopt what may be broadly thought of as pro-cable distribution policies, may be further enhanced.

234. To a certain extent, the potential for such conduct may have been limited by the Commission's recent decision amending its program carriage (as distinguished from the program access) rules.[561] The Commission has amended its rules to provide standing to MVPDs to file a complaint alleging that a cable operator has coerced a programmer, whether affiliated or not, into granting exclusivity to the cable operator.[562]

235. Other Entry Deterring Behavior. The record also reflects several other types of strategic behavior allegedly engaged in by cable operators that may have the effect of

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[558] *See supra* Section IV.B.2.a.

[559] *See supra* ¶¶ 182-83.

[560] *See supra* ¶¶ 179-180.

[561] *Carriage Mem. Opinion & Order* (MM Docket No. 92-265).

[562] *Id.* ¶ 40, App. A.

raising rivals' costs and thereby deterring competitive entry. For example, one SMATV commenter complains that a competing cable operator purposely impedes subscriber changeovers by failing to disconnect subscribers in a timely manner and refuses to coordinate the process with the alternative provider.[563]

236. In addition, there are allegations in the record of cable operators engaging in conduct that may impede the ability of MMDS operators to acquire needed licenses. In particular, it is claimed that cable operators have induced ITFS licensees not to lease their excess capacity to wireless cable operators.[564]

237. A final type of strategic behavior that may serve to delay entry and raise rivals' costs is the aggressive use of the legal process. For example, TCI filed a civil action seeking to overturn the award of a second franchise to Fibervision by the state of Connecticut. At the time the suit was filed one published report suggested that the suit could delay Fibervision's construction schedule and complicate its ability to raise financing.[565] That suit has recently been resolved in Fibervision's favor.[566] In a second situation, Warner Cable, a predecessor to Time Warner, filed various legal challenges which delayed the planned construction by the city of Niceville, Florida of a municipal overbuild. In one of these cases, the Supreme Court of the State of Florida rejected Warner's challenge to a lower court order authorizing the city to issue revenue bonds to construct the municipal overbuild.[567] In a second case, the Eleventh Circuit affirmed the lower court's rejection of Warner Cable's challenge to the municipal overbuild.[568] Despite these court victories, one published report noted that Niceville still had not begun construction of its system as of 1993.[569]

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[563] Liberty Cable Comments at 16-17.

[564] *See supra* ¶¶ 85-86.

[565] Geoffrey Foisie, *TCI Goes To Court to Block Overbuild,* BROADCASTING & CABLE, Apr. 25, 1994, at 38; Anthony Giorgianni, *Cable Company Complains Competitor Given an Edge*, THE HARTFORD COURANT, Apr. 1, 1994, at B1.

[566] *Overbuild Appeal Denied*, BROADCAST & CABLE TELEFAX, Sept. 13, 1994.

[567] *Warner Cable Communications v. City of Niceville*, 520 So. 2d 245 (Fla. 1988).

[568] *Warner Cable Communications v. City of Niceville*, 911 F.2d 634 (11th Cir. 1990), *cert. denied*, 501 U.S. 1222 (1991).

[569] Bob Boyle, *Florida Municipal Overbuilders in Wait Mode,* MULTICHANNEL NEWS, Oct. 18, 1993, at 37; Bell Atlantic Comments at 4 n.6.

238. The filing of sham litigation has long been recognized as a means of raising rivals' costs that is actionable under the antitrust laws.[570] On the other hand, such claims may have a legitimate basis (beyond deterring entry), and, therefore, constitute protected conduct. For example, Time Warner commented that actions it brought against Niceville to enjoin construction of a municipal overbuild were not a "delaying tactic," as asserted by Bell Atlantic.[571] Rather, Time Warner claims that it initiated the litigation to vindicate its due process and First Amendment rights.[572]

b. Regulatory Impediments

239. The record in this proceeding also reflects various regulatory impediments to competitive entry. One regulatory impediment to SMATV and wireless entry arises from the Communications Act's definition of a "cable system." As discussed herein, a SMATV or wireless system that connects separately owned buildings with a wire (even if the wire does not cross a public right-of-way) is deemed a "cable system" under the Communications Act and would be required to obtain a local franchise.[573] As an alternative to submitting to the franchising process, operators either use more-expensive microwave relays to distribute between adjacent buildings or forego service to the buildings altogether.

240. The record also reflects federal statutory schemes that prevent competitive entry altogether, or may prevent the most efficient form of entry. More importantly, under the Communications Act, LECs are prohibited from providing video programming directly to subscribers in their service areas. The Commission has established a VDT model by which LECs can operate broadband video distribution systems on a common carrier basis, consistent with this cable-telco ownership ban.[574] However, conditioning LEC entry on the provision of common carrier services may affect the manner in which LECs can most efficiently enter the market. For this reason, the Commission continues to advocate repeal of the cable-telco cross-ownership ban, subject to the imposition of appropriate safeguards to prevent cross-subsidization from local exchange services.[575]

241. Various state laws may also serve to impede competitive entry. For example, a recently enacted California statute allows municipalities to require video programming

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[570] *See, e.g., MCI Communications Corp. v. AT&T*, 708 F.2d 1081, 1156 (7th Cir.), *cert. denied*, 464 U.S. 891 (1983).

[571] *See* Bell Atlantic Comments at 4 & n.6; Time Warner Reply Comments at 11, n.12.

[572] Time Warner Reply Comments at 11 n.12.

[573] *See supra* ¶ 88.

[574] *See supra* ¶ 104.

[575] *Telco-Cable First Report & Order* ¶¶ 44-46, 7 FCC Rcd at 322-23.

distributors to undertake various actions in cities in which they offer video programming.[576] That requirement will potentially impose significant costs on alternative distributors. Similarly, despite limited preemption by the Commission,[577] local zoning regulations may inhibit competition from direct-to-home programming distributors, by preventing home users from installing HSDs and smaller DBS dishes.

c. Potential Technological Bottlenecks

242. The creation of technological bottlenecks in the telecommunications industry, historically, has been of great concern to the Commission. The record in this proceeding reflects a variety of potential bottlenecks, some as old as the industry itself, and others related to emerging technological developments.

243. In particular, concerns have recently reemerged with respect to utility poles as a potential bottleneck where cable operators themselves might be suffering competitive harm.[578] Many cable operators lease space on utility poles in order to string wires and deliver programming. The contract between the cable operator and the owner of the pole is known as a "pole attachment agreement." "[A]s a solution to a perceived danger of anticompetitive practices by utilities in connection with cable television service,"[579] Congress passed the Pole Attachments Act of 1978, which directs the Commission, with certain exceptions, to ensure that the "rates, terms and conditions [of such agreements] are just and reasonable . . . ."[580] At this juncture, the Commission notes that pole attachment is an area that could affect the status of competition in the delivered video programming market and may merit Commission attention in the future.[581]

244. The Commission notes that MSOs are currently investing in digital compression and encryption technologies, which could impact the manner in which "raw" video programming is distributed via satellite nationally, and possibly create a technological bottleneck to competing distribution media. For example, two commenters have expressed concern that TCI's National Digital Television Center might be used to block access to

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[576] 5 CAL. GOV. CODE 1(a) §§ 53088.1-2.

[577] *See supra* ¶ 76.

[578] *See, e.g., Selkirk Communications, Inc. v. Florida Power & Light Co.*, 8 FCC Rcd 387 (1993); *Heritage Cablevision Assocs. v. Texas Elec. Co.*, 8 FCC Rcd 373, *appeal denied sub nom., Tex. Elec. Co. v. FCC*, 997 F.2d 925 (D.C. Cir. 1993).

[579] *FCC v. Florida Power Corp.*, 480 U.S. 245, 247 (1987).

[580] 47 U.S.C. § 224(b)(1).

[581] The Commission did not seek or receive public comment on the issue of pole attachments in this proceeding. Accordingly, this *Report* makes no conclusions concerning the status of this issue or the need for Commission or congressional action.

programming by competing MVPDs.[582] That facility would convert the analog feeds of participating programmers into a compressed and encrypted digital format and then uplink the feed to satellites for distribution to cable systems and home satellite users.[583] Commenters appear to be concerned that, over time, access to the Digital Television Center may become necessary in order to gain access to programming that is encrypted through that facility.[584]

245. Finally, as the cable industry converts to digital technology and two-way communications, issues concerning network architecture, standardization, and access may become important competitive issues as they have in the telephone industry. While this *Report* provides no analysis of the potential significance of such issues at this time, it is likely that such issues will require attention in future *Reports*.[585]

4. *Extent of Competition in the Multichannel Video Programming Distribution Market*

246. Today, most local markets for multichannel video programming distribution services are supplied by monopoly cable systems. At present, competitive rivalry in most local multichannel video programming distribution markets is largely, often totally, insufficient to constrain the market power of incumbent cable systems. As the overbuild experience demonstrates, the entry of competitors to local cable systems over the coming months and years should exert a significant, favorable effect on market conduct and performance in local markets for multichannel video distribution services. Consequently, the outlook for improved market performance in multichannel video programming distribution markets as a consequence of increasing competitive rivalry remains promising.

B. Future Considerations and Recommendations for Promoting Competition to Cable Systems

247. The Commission has, throughout this *Report*, identified several types of dominant firm strategic behavior, policy-relevant barriers to entry, and technological bottlenecks that could adversely affect performance in the multichannel video programming distribution market. The Commission has noted in this *Report* that several alternative distribution media are just now becoming operational and available to a significant number of

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[582] *See* WCA Reply Comments at 3-4; Direct TV Comments at 7-8.

[583] *See, e.g.*, Peter Lambert, *MSOs Split on TCI's Headend in the Sky*, MULTICHANNEL NEWS, Mar. 28, 1994, at 1; Kate Maddox, *TCI Opens New Digital Tech Center*, ELECTRONIC MEDIA, Apr. 11, 1994, at 4; Cherian George, *Cable TV Stays Ahead with Technology*, THE STRAITS TIMES, May 5, 1994, at 7.

[584] WCA Comments at 3-4.

[585] Recent papers that address such issues from an economic perspective may be found in Symposium on Compatibility, 40 J. INDUS. ECON. 1-123 (Richard J. Gilbert ed. Mar. 1992).

consumers. In particular, the nation's first high-powered DBS operators, DirecTV/USSB, which project that there will be five to ten million households receiving DBS services by the end of the decade, have only become operational within the last six months.[586] Moreover, LECs hope to make available networks that are capable of delivering video programming to over twenty million subscribers by the end of the decade.[587] However, while numerous LECs are engaged in various trials of VDT service, such service has been authorized in only a single market. As a result, while the Commission believes that several specific reforms might improve market performance, most of the competitive issues raised in this *Report* will require ongoing monitoring as a more dynamic and competitive environment develops in this market.

248. The Commission's procedures for "effective competition" challenges to rate regulation are not designed to, and do not, provide enough information to monitor the extent of competitive entry on a nationwide scale.[588] In the coming year, Commission staff will endeavor to find a mechanism to collect, interpret and monitor the growth of alternative distribution media so future *Reports* will be able to provide a more complete picture of the status of competition at both the local and national levels.

249. In particular, consistent with the 1992 Cable Act's policy of encouraging cable overbuilding, the Commission will continue to collect data and information regarding the extent of cable overbuilding and the competitive checks that overbuilds have on the pricing behavior of incumbent cable systems.

250. The Commission will also monitor whether undue delays in granting final determinations on overbuild franchise applications interfere with the effectiveness of Section 621 of the Communications Act, which prohibits a franchising authority from refusing to grant a competitive franchise. Section 621 provides an applicant with the right to appeal the denial of an application to the Commission, but only from the "final" decision or determination of a franchising authority.[589]

251. In addition, the Commission will continue to monitor litigation involving the application of the Congressional ban on the granting of exclusive cable franchises to existing situations. The Commission believes that the approach of the Eleventh Circuit in *Cox Cable Communications, Inc. v. United States*[590] correctly interprets the statute, but notes the

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[586] USSB Comments at 2, 8; DirecTV Comments at 1, 16.

[587] *See supra* ¶ 118.

[588] *See supra* ¶¶ 51-53.

[589] *See supra* ¶ 56.

[590] 992 F.2d 1178 (11th Cir. 1993).

inconsistent holding of the court in *Jones Cable Partners v. City of Jamestown*.[591] If the holding of the *Jones* court gains approval in a United States Circuit Court of Appeals, the Commission will recommend that Congress revise Section 621 of the Communications Act to provide a clear expression of Congressional intent to have the provision apply to existing exclusive franchise agreements.

252. The Commission recommends that Congress consider modifying 47 U.S.C. § 522(7)(B) so as to exclude from the definition of a "cable system" not only commonly-owned, but also separately-owned, dwellings interconnected by wires which do not cross public rights-of-way. Such a revision would promote the growth of wireless cable and SMATV systems as competitors to cable systems by substantially reducing the costs of expanding their systems.

253. Besides these specific proposals, however, there are several other issues of strategic behavior, barriers to entry, and technological bottlenecks that the Commission believes merit future study through this annual report process. Because this market is dynamic and evolving, the Commission anticipates that, to a certain extent, this series of reports will be a work in progress in which certain parts are continually updated and revised.

254. At present, the Commission expects the following issues to be among those covered in next year's and subsequent competition reports: (a) changes and trends in cable industry performance; (b) the status of competing technologies; (c) horizontal concentration of MSOs, cable operator ownership of other distribution technologies, and investments by firms outside the cable industry, such as LECs, in the cable industry; (d) vertical relationships between MVPDs and programming interests; and (e) emerging technological advances, such as digital compression and encryption, and their impact on the cost structure for providers of video programming, and the potential creation of barriers or "bottlenecks." Future reports will also continue to provide updated information concerning application of the program access and program carriage rules administered by the Commission, as well as continuing analyses of the evolution of contracting practices between programmers and MVPDs in response to those rules. Finally, the Commission will report information regarding the number and character of cable systems deemed to be in "effective competition," and therefore no longer subject to rate regulation.

255. Because of these recurring issues, the Commission stated in its *NOI* that "it may be desirable to establish more systematic reporting procedures,"[592] and requested the industry to comment on the methods the Commission might use in the future to gather information. In particular, the Commission requested comment on whether surveys or questionnaires of MVPDs and video programmers would be an appropriate method of updating the various tables attached to this *Report*; whether the Commission should institute annual reporting requirements for all or some MVPDs as a method of tracking and evaluating

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[591] 822 F. Supp. 476 (M.D. Tenn. 1993). *See supra* note 126.

[592] *NOI* ¶ 78, 9 FCC Rcd at 2908.

the development of competition in the video programming marketplace; and how information on vertical relationships between cable systems and video programmers (already maintained pursuant to 47 C.F.R. § 76.504(e)) could be compiled and maintained for use by the Commission in these reports.[593] The Commission also sought comments concerning whether the information compiled pursuant to the *Primestar Consent Decrees* should be made available to the Commission,[594] and how the Commission could gather or examine proprietary or confidential data and protect information that is obtained.[595]

256. Several commenters note that a majority of the basic information sought by the Commission generally is available through public sources, such as company reports filed with the Securities and Exchange Commission, and the publications of Paul Kagan Associates Inc., NCTA and SBCA.[596] In addition, commenters state that the Commission will obtain pertinent information, such as data on industry pricing, through rate and program access complaints.[597] The majority of the commenters oppose as burdensome the imposition of any additional mandatory reporting requirements.[598] Several commenters also express concern about the collection of confidential and proprietary business information.[599] Some commenters dispute

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[593] *Id.* ¶¶ 79-80, 9 FCC Rcd at 2908-09.

[594] *NOI* ¶¶ 86-87, 9 FCC Rcd at 2909-10. Viacom contends that it would be inappropriate for the Commission to compel disclosure of the information required by the *Primestar* Decrees, as this would discourage parties from entering into such agreements. Viacom Reply Comments at 4.

[595] *NOI* ¶¶ 88-89, 9 FCC Rcd at 2910.

[596] *See* NCTA Comments at 29-30; Liberty Media Comments at 14-15; SBCA Comments at 14-15, Appendix A; Viacom Reply Comments at 4.

[597] TCI Comments at 14; Liberty Media Comments at 15; PrimeTime 24 Reply Comments at 4-5.

[598] *See* TWC Comments at 37. *See also* TCI Comments at 14-15; Liberty Media Comments at 14; WCA Comments at 27-28 (wireless operators do not keep data on their wired competitors).

[599] *See, e.g.*, TWC Comments at 37-38; HBO Comments at 21; PrimeTime 24 Reply Comments at 4. GTE contends that any reporting requirements should be kept to a minimum, should be phased out when video distribution markets are found to be competitive, and should be collected from programmers in order to avoid double-counting of subscribers. GTE Comments at 3, 6, 9-10.

whether the Commission even has the authority to impose such reporting requirements.[600] In contrast, a few commenters favor some form of reporting requirements.[601]

257. The Commission believes that Sections 19(f)(2) and 3(g) of the 1992 Cable Act,[602] as well as its licensing authority and other sections of the Communications Act,[603] provide a sufficient legal basis for the Commission to establish and impose reporting requirements with respect to MVPDs and vertically-integrated programming vendors. However, the Commission is sensitive to the concerns expressed by the cable industry and others regarding the imposition of additional and costly administrative burdens. The Commission also is sensitive to the concerns of the industry regarding proprietary and confidential information.

258. Consequently, at this time, the Commission will not recommend any additional reporting requirements to facilitate preparation of future competition *Reports*. At present, for its next report, the Commission intends to develop information through a new notice of inquiry and submitted comments, limited voluntary surveys, and publicly-available information from trade and industry sources. The Commission will also review information already filed with the Commission, such as information provided in rate and program access complaints. In addition, as described above, Commission staff will endeavor to find a mechanism other than certification challenges to determine the extent of effective competition to cable nationwide.

259. Consistent with the requirement that the Commission annually report to Congress on the status of competition, future reports will be submitted to Congress by November 15 of each subsequent year.

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[600] HBO Comments at 19-21; TCI Comments at 13-14; TWC Reply Comments at 28-29; PrimeTime 24 Reply Comments at 3; *but see* Viacom Reply Comments at 4 (Commission "has ample authority" to collect data "in the context of a specific enforcement or investigative proceeding").

[601] NRTC Comments at 25-27; CSS Comments at 6; DirecTV Comments at 22; Bell Atlantic Comments at 10-11.

[602] 47 U.S.C. §§ 548(f)(2), 543(g).

[603] *See, e.g.*, 47 U.S.C. §§ 154(i), 308(b), 403.

VI.
ADMINISTRATIVE MATTERS

260. This *Report* is issued pursuant to authority contained in Section 19(g) of the Cable Television Consumer Protection and Competition Act of 1992, 47 U.S.C. § 548(g), and Sections 4(i) and 403 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 403.

261. It is ORDERED that the Secretary shall send copies of this *Report* to the appropriate committees and subcommittees of the United States House of Representatives and the United States Senate.

Federal Communications Commission

William F. Caton
Acting Secretary

APPENDIX A

Notice of Inquiry, Docket No. CS 94-48

Comments		Date received
1.	Bell Atlantic	(6/29/94)
2.	BellSouth Telecommunications, Inc.	(6/29/94)
3.	CellularVision of New York, L.P.	(6/29/94)
4.	Consumer Satellite Systems, Inc., Programmers Clearing House, Inc., and Satellite Receivers, Ltd.	(6/29/94)
5.	DirecTV, Inc.	(6/29/94)
6.	GTE Service Corporation	(6/29/94)
7.	Home Box Office	(6/29/94)
8.	Liberty Cable Company, Inc.	(6/29/94)
9.	Liberty Media Corporation	(6/29/94)
10.	National Cable Television Association, Inc.	(6/29/94)
11.	National Rural Telecommunications Cooperative	(6/29/94)
12.	NYNEX Telephone Companies	(6/29/94)
13.	Peoples Choice TV Corporation	(6/29/94)
14.	Primestar Partners, L.P.	(6/29/94)
15.	Satellite Broadcasting and Communications Association of America	(6/29/94)
16.	Tele-Communications, Inc.	(6/29/94)
17.	Time Warner Cable	(6/29/94)
18.	Turner Broadcasting System, Inc.	(6/29/94)
19.	US West Communications, Inc.	(6/29/94)
20.	Wireless Cable Association International, Inc.	(6/29/94)

Reply Comments		Date received
1.	American Telecasting, Inc.	(7/29/94)
2.	Ameritech	(7/29/94)
3.	Bell Atlantic	(7/29/94)
4.	Comedy Partners	(7/29/94)
5.	Consumer Satellite Systems, Inc., Programmers Clearing House, Inc. and Satellite Receivers, Ltd.	(7/29/94)
6.	GTE Service Corporation	(7/29/94)
7.	Home Box Office	(7/29/94)
8.	Liberty Cable Company, Inc.	(7/29/94)
9.	National Cable Television Association, Inc.	(7/29/94)
10.	National Rural Telecommunications Cooperative	(7/29/94)
11.	Netlink USA	(7/29/94)
12.	Primestar Partners, L.P.	(7/29/94)
13.	Primetime 24	(7/29/94)
14.	Southern Satellite Systems, Inc	(7/29/94)

15. Superstar Satellite Entertainment . . . . . (7/29/94)
16. Teledesic Corporation . . . . . (7/29/94)
17. Time Warner Cable . . . . . (7/29/94)
18. United States Satellite Broadcasting Company, Inc., Consolidated Comments and Reply Comments . . . . . (7/29/94)
19. Valuevision International, Inc. . . . . (7/29/94)
20. Viacom International Inc. . . . . (7/29/94)
21. Wireless Cable Association International, Inc. . . . . (7/29/94)

Miscellaneous Filings	Date Received
1. Errata to NCTA's Comments filed June 29, 1994 (with attachments)	(7/25/94)
2. Letter from Deborah C. Costlow, Esq. to Cable Services Bureau Staff . . .	(8/12/94)
3. Letter from Deborah C. Costlow, Esq. to Cable Services Bureau Staff . . .	(8/23/94)
4. USSB - Supplement to Consolidated Comments and Reply Comments . . .	(8/19/94)
5. NRTC Letter Response to USSB Supplement	(9/02/94)
6. USSB Response to Commission Request	(9/13/94)
7. DirecTV Letter Response to Commission Request	(9/12/94)

Note: The Commission also received numerous letters in support of the NRTC's Comments in this proceeding.

APPENDIX B

GLOSSARY OF TECHNICAL TERMS AND ACRONYMS

Asynchronous Digital Subscriber Line ("ADSL") - A technology that utilizes compression of digital video signals to enable existing copper twisted pairs to carry multiple, simultaneous high-speed services to the subscriber.

Asynchronous Transfer Mode ("ATM") - An international standard set by the Consultative Committee on International Telegraph and Telephone ("CCITT") for high-speed broadband transport of packet-switched networks operating at specified digital transmission speeds. ATM switches facilitate efficient operation of networks transporting "bursts" of information that may include video signals. *See* Telecom Publishing Group, *Telecom Lingo Guide* 6 (6th ed. 1991).

Broadband - A term used to describe any system capable of delivering multiple channels or services to its users.

Broadband Switch - A term used to refer to a technology designed to route broadband signals through a transmission system. ATM is a type of broadband switch.

Channel Service - A service whereby Local Exchange Carriers offer, on a common carrier basis, complete video transport services to cable operators from a cable system's headend to residential customers' premises. *Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54-63.58, Further Notice of Proposed Rulemaking, First Report and Order and Second Further Notice of Inquiry* ¶ 11, 7 FCC Rcd 300, 307 (1991).

Fiber to the Curb ("FTTC") - A type of architecture involving the installation of fiber optic cable from the trunk through the distribution network to the curb. A curbside "vault" typically will serve a dozen homes.

Fiber to the Home ("FTTH") - A type of architecture involving the installation of fiber optic cable throughout the network from the trunk to end-user premises.

Fiber to the Node ("FTTN") - A type of architecture involving the installation of fiber optic cable from the trunk, through the distribution network, to the neighborhood or the node. Typically, a node will serve between 400 and 500 homes.

Hybrid Fiber-Coax ("HFC") - A type of architecture involving the installation of fiber through part of the distribution network, with coaxial cable installed in the remainder of the network to the end-user. HFC architecture is generally used with either FTTC or FTTN, with coax replacing conventional copper wire to the end-user.

Instructional Television Fixed Service ("ITFS") - A fixed microwave station operated by an educational organization and used mainly to transmit educational information to fixed

receiving stations. Wireless cable operators have access to the channels allocated to ITFS on a leased, part-time basis. PUBLIC SERVICE DIVISION, FEDERAL COMMUNICATIONS COMM'N, COMMUNICATIONS GLOSSARY 10 (1993).

InterLATA - Telecommunications services that originate and terminate in different Local Access and Transport Areas ("LATAs").

Local Access and Transport Area - Contiguous local exchange areas developed in connection with the divestiture of AT&T within which Bell Operating Companies ("BOCs") may provide service. Pursuant to the Modification of Final Judgment ("MFJ"), BOCs are not permitted to transport calls across LATA boundaries but rather must connect them to interexchange carriers.

Local Exchange Carrier ("LEC") - Carrier which transports calls within a local exchange area and provides customers access to long distance telecommunications services. The term is sometimes used to refer to the Bell Operating Companies and other local telephone companies.

Modified Final Judgment ("MFJ") - Agreement between AT&T and the Department of Justice which, as amended by the federal courts, effected divestiture and imposed various restrictions on the Regional Bell Operating Companies (RBOCs). *United States v. AT&T*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983). See also LELAND L. JOHNSON, TOWARD COMPETITION IN CABLE TELEVISION 192 (1994).

Motion Picture Experts Group ("MPEG") - A group within the International Standards Organization that developed the digital compression standard for voice and video.

Multiplex - To transmit multiple signals over a single channel.

National Television System Committee ("NTSC") - A committee comprised of industry representatives that established the NTSC standard for black-and-white television in 1940, and color television in the early 1950s.

Optical Digital Loop Carrier System - System of routing calls through fiber optic cable originating from the central office of the LEC to remote distribution units. From these units, a conventional copper loop is used to connect subscriber premises.

Trunk - A single transmission channel between two points that are usually switching centers.

APPENDIX C[1]

TABLE 1:
Cable Television Industry Growth, 1987-93

	1987	*1990*	*1993*	*% change '87-'90*	*% change '90-'93*
U.S. Television Households ("HH") (mil.)*	88.6	92.6	96.4	4.51%	4.10%
Homes Passed ("HP") (mil.)	73.1	86	92.9	17.65%	8.02%
Basic Subscriptions at Year End ("subs") (mil.)	42.6	51.7	57.4	21.36%	11.03%
National Saturation (HP/HHs) (%)	*82.51%*	*92.87%*	*96.37%*	*12.57%*	*3.77%*
Percentage of TV Households subscribing (%)	*48.08%*	*55.83%*	*59.54%*	*16.12%*	*6.65%*
Mean US Penetration (subs/HP) (%)	*58.28%*	*60.12%*	*61.79%*	*3.16%*	*2.78%*

* U.S. Television Households from A.C. Nielsen Co. as of January of the year following that listed. WARREN PUBLISHING, INC., 1988 CABLE TELEVISION FACTBOOK C-314, WARREN PUBLISHING, INC., 1991 CABLE TELEVISION FACTBOOK C-344, WARREN PUBLISHING, INC., 1994 CABLE TELEVISION FACTBOOK F-1.

Source: *History of Cable & Pay TV Subscribers & Revenues,* CABLE TV INVESTOR, March 31, 1994, at 9.

[1] For the tables that appear in this Appendix of the *Report*, the Commission has chosen to display information for three years -- 1987, 1990 and 1993. The year 1990 was chosen because it was the last time the Commission reported to Congress on the status of competition in the industry, and 1993 was chosen because it is the most recent year for which information is generally available. Accordingly, the rate of change is measured over a three-year period, and 1987 was chosen to provide a three-year period to be used as a basis for comparison.

TABLE 2:
Channel Capacity of Cable Systems, 1987-93

Channel Capacity	*1987**		*1990**		*1993**	
	Number of systems	*Percent of systems***	*Number of systems*	*Percent of systems***	*Number of systems*	*Percent of systems***
54 and over	565	8.01%	808	9.60%	1,306	13.13%
30 to 53	3,272	46.40%	4,846	57.55%	6,364	63.96%
20 to 29	1,298	18.41%	1,370	16.27%	1,197	12.03%
13 to 19	312	4.42%	283	3.36%	364	3.66%
6 to 12	1,557	22.08%	1,081	12.84%	697	7.01%
5 or less	48	0.68%	32	0.38%	22	0.22%
Not available	784		1,192		1,210	
Total	7,836		9,612		11,160	
Subtotal 30 plus	***3,837***	***54.41%***	***5,654***	***67.15%***	***7,670***	***77.09%***
Subtotal 29 or less	***3,215***	***45.59%***	***2,766***	***32.85%***	***2,280***	***22.91%***

* Figures are as of April 1, 1987, April 1, 1990 and November 1, 1993.
** Percentage does not include systems for which information was not available
Sources: WARREN PUBLISHING, INC., 1987 TELEVISION AND CABLE FACTBOOK A-41; WARREN PUBLISHING, INC., 1990 TELEVISION AND CABLE FACTBOOK C-385; WARREN PUBLISHING, INC., 1994 TELEVISION AND CABLE FACTBOOK F-3.

TABLE 3:
Channel Capacity for Subscribers, 1987-1993

Channel Capacity	*1987**		*1990**		*1993**	
	Number of subs.	*Percent of subs.***	*Number of subs.*	*Percent of subs.***	*Number of subs.*	*Percent of subs.***
54 and over	5,752,221	15.09%	11,677,066	24.42%	20,909,256	38.37%
30 to 53	24,099,718	63.21%	31,765,994	66.44%	31,712,387	58.20%
20 to 29	5,439,395	14.27%	3,540,389	7.41%	1,482,527	2.72%
13 to 19	501,109	1.31%	180,199	0.38%	117,713	0.22%
6 to 12	2,232,808	5.86%	638,207	1.33%	262,010	0.48%
5 or less	102,394	0.27%	7,234	0.02%	3,254	0.01%
Not available	634,601		804,350		636,731	
Total	38,762,246		48,613,439		55,123,878	
Subtotal 30 plus	***29,851,939***	***78.29%***	***43,443,060***	***90.87%***	***52,621,643***	***96.58%***
Subtotal 29 or less	***8,275,706***	***21.71%***	***4,366,029***	***9.13%***	***1,865,504***	***3.42%***

* Figures are as of April 1, 1987, April 1, 1990 and November 1, 1993.
** Subs. = subscribers; percentages calculated based on totals that excluded subscribers for whom information was not available.
Sources: WARREN PUBLISHING, INC., 1987 TELEVISION AND CABLE FACTBOOK A-41; WARREN PUBLISHING, INC., 1990 TELEVISION AND CABLE FACTBOOK C-385; WARREN PUBLISHING, INC., 1994 TELEVISION AND CABLE FACTBOOK F-3.

TABLE 4:
Growth By Network Type

Network Type	1987 no. of netw'ks	1987 % of all netw'ks	1990 no. of netw'ks	1990 % of all netw'ks	1993 no. of netw'ks	1993 % of all netw'ks	'87-'90 % change	'90-'93 % change
Basic/No-Charge	59	78.67%	61	79.22%	72	72.73%	3.39%	18.03%
Premium	9	12.00%	5	6.49%	9	9.09%	-44.44%	80.00%
Pay Per View	6	8.00%	7	9.09%	13	13.13%	16.67%	85.71%
Combination	1	1.33%	4	5.19%	5	5.05%	300.00%	25.00%
Total	*75*		*77*		*99*		*2.67%*	*28.57%*

* A decline in the number of networks of a given type does not necessarily imply that those networks exited the market. It is equally as likely that several of the networks changed the nature of their services (and became "combination" networks, for example).

Source: *National Cable Video Networks by Type of Service,* CABLE TELEVISION DEVELOPMENTS (National Cable Television Association), Apr. 1994, at 7-A.[2]

TABLE 5:
Source of Revenue

Source of Revenue	1987 $ mil.	1987 % of total	1990 $ mil.	1990 % of total	1993 $ mil.	1993 % of total	1987-90 % chg growth	1990-93 % chg growth
Basic Subscription Revenue	6,014	51.12%	10,169	56.95%	13,552	59.07%	69.09%	33.27%
Pay revenue	4,112	34.95%	5,105	28.59%	4,633	20.19%	24.15%	-9.25%
Expanded Basic Revenue	377	3.20%	495	2.77%	1,641	7.15%	31.30%	231.52%
Advertising Revenue	264	2.24%	628	3.52%	1,064	4.64%	137.88%	69.43%
Installation Revenue	241	2.05%	289	1.62%	289	1.26%	19.92%	0.00%
Pay-per-view Revenue	86	0.73%	253	1.42%	512	2.23%	194.19%	102.37%
Home Shopping Revenue	57	0.48%	72	0.40%	128	0.56%	26.32%	77.78%
Miscellaneous Revenue	613	5.21%	845	4.73%	1,123	4.89%	37.85%	32.90%
Total Revenue	*11,764*		*17,856*		*22,942*		*51.79%*	*28.48%*

Source: *History of Cable & Pay TV Subscribers & Revenues,* CABLE TV INVESTOR, March 31, 1994, at 9; 1993 revenue from advertising (and accordingly, total revenue) adjusted based on Kathy Healy, *Marketers Tune in to Cable's Appeal; Improvements Lead to Big Gains in Ad Spending,* ADVERTISING AGE, Feb. 28, 1994, at C-3.

[2] The total number of programming networks for 1990 shown in this table reflects the total at the end of 1990, and differs from the total number of networks shown in *1990 Cable Report*, App. G, Tbls. 4-5, which were derived from information obtained in 1988 and 1989.

TABLE 6:
Cable Industry Expenditure On Programming, 1987-1993

Expenditure Type	*1987 (millions)*	*1990 (mil.)*	*1993 (mil.)*	*87-90 % change*	*90-93 % change*
*Basic Programming	$572	$1,410	$2,187	146.50%	55.11%
Other Programming	$1,717	$1,785	$1,813	3.96%	1.57%
***All Programming*	*$2,289*	*$3,195*	*$4,000*	*39.58%*	*25.20%*

Sources: * Paul Kagan Associates, Inc., MARKETING NEW MEDIA, March 15, 1993, p. 1; Paul Kagan Associates, Inc., MARKETING NEW MEDIA, June 20, 1994, p. 1; ** *Cable Systems' Programming Expenditures*, CABLE TELEVISION DEVELOPMENTS 7-A (National Cable Television Association Apr. 1994).

TABLE 7:
Cash Flow Figures of Cable System Operators[3]

*Cable System Operators with Publicly Available Figures**	*1987*			*1990*			*1993*		
	cash flow (mil.)	*cash flow per sub.*	*cash flow margin*	*cash flow (mil.)*	*cash flow per sub.*	*cash flow margin*	*cash flow (mil.)*	*cash flow per sub.*	*cash flow margin*
Tele-Communications, Inc. (1)	$773	$117.05	43.35%	$1,259	$147.68	42.79%	$1,858	$178.55	44.74%
Time Warner Cable (2)**	$527	$103.23	38.16%	$769	$118.75	43.92%	$1,035	$143.45	46.88%
Comcast Cable (4)	$117	$107.83	40.77%	$264	$161.27	44.59%	$552	$208.46	50.41%
Cablevision Systems (5)	$92	$117.95	30.67%	$241	$154.98	42.81%	$281	$130.82	44.39%
Cablevision Industries (8)	-	-	-	$135	$130.56	45.15%	$192	$153.11	48.36%
Times Mirror Cable (9)	$78	$84.87	32.50%	$141	$130.68	38.01%	$202	$158.56	42.98%
Jones Intercable (10)	$103	$105.21	46.40%	$183	$128.78	45.41%	$187	$148.06	41.56%
Adelphia Communications (11)	$55	$94.66	55.56%	$131	$126.82	56.96%	$173	$139.07	56.72%
Viacom (12)	$108	$102.08	38.16%	$143	$135.16	43.33%	$182	$166.36	43.75%
Falcon Cable TV (14)***	$10	$111.11	50.00%	$20	$115.61	51.28%	$27	$146.74	50.00%
Century Communications (15)	$60	$85.11	54.55%	$123	$142.20	56.16%	$177	$187.30	49.03%
E.W. Scripps (19)****	-	-	-	$34	$129.77	-	$105	$149.57	40.38%
Post-Newsweek Cable (25)	$40	$103.90	40.40%	$63	$144.50	43.45%	$82	$170.12	44.09%
TCA Cable (26)	$30	$88.76	50.00%	$61	$130.06	53.51%	$78	$164.90	51.32%
Multimedia Cablevision (30)	$42	$137.70	46.15%	$60	$171.43	50.00%	$85	$203.84	51.52%
Total for Group	***$2,035***	***$107.48***	***40.90%***	***$3,627***	***$137.53***	***44.19%***	***$5,216***	***$164.29***	***46.14%***
Total for Industry**	***$4,812***			***$7,890***			***$10,549***		

* Displayed in descending order according to 1993 total basic subscribers, with the company's rank relative to all systems following in parenthesis.

** Includes both American Tel. & Communications Corp. (Time, Inc.) and Warner Cable Communications for 1987 and 1990, before the two were completely merged.

*** Includes only Falcon Cable Systems, a division of Falcon Cable TV.

**** The 1990 figures for E.W. Scripps are not included in the measure of change between 1987 and 1990.

***** Total estimate for industry cash flow was calculated by muliplying the estimated industry total revenue by cash flow margin for the group of companies.

Sources: 1993 Annual Reports for listed companies; PAUL KAGAN ASSOCIATES, INC., THE CABLE TV FINANCIAL DATABOOK 14-15, 37, 62 (1994); PAUL KAGAN ASSOCIATES, INC., THE CABLE TV FINANCIAL DATABOOK 17-18, 41, 66 (1991); PAUL KAGAN ASSOCIATES, INC., THE KAGAN CABLE TV FINANCIAL DATABOOK 20-21, 28-59, 86 (1991); *History of Cable & Pay TV Subscribers & Revenues,* CABLE TV INVESTOR, March 31, 1994, at 9; Tom Kerver, *Cablevision's Top 200,* CABLEVISION, May 23, 1994, at 101-123.

[3] The term cash flow is used in Tables 7 and 8 to refer to the measurement of earnings before accounting for interest payments, taxes, depreciation and amortization ("EBITDA). The group of companies that is used in both Table 7 and Table 8 includes 7 of the 10 largest cable system operators in terms of basic subscribers served in 1993, and 15 of the 30 largest such companies. Those fifteen MSOs are the fifteen largest MSOs for which information was publicly available.

TABLE 8:
Cable MSOs' Revenues and Subscriber Totals[4]

*Cable System Operators with Publicly Available Figures***	*1987*		*1990*		*1993*	
	basic subs. (000)*	*cable revenue (mil.)*	*basic subs. (000)*	*cable revenue (mil.)*	*basic subs. (000)*	*cable revenue (mil.)*
Tele-Communications, Inc. (1)	6,604	$1,783	8,525	$2,942	10,406	$4,153
Time Warner Cable (2)***	5,105	$1,381	6,476	$1,751	7,215	$2,208
Comcast Cable (4)	1,085	$287	1,637	$592	2,648	$1,095
Cablevision Systems (5)	780	$300	1,555	$563	2,148	$633
Cablevision Industries (8)	-	-	1,034	$299	1,254	$397
Times Mirror Cable (9)	919	$240	1,079	$371	1,274	$470
Jones Intercable (10)	979	$222	1,421	$403	1,263	$450
Adelphia Communications (11)	581	$99	1,033	$230	1,244	$305
Viacom (12)	1,058	$283	1,058	$330	1,094	$416
Falcon Cable TV (14)****	90	$20	173	$39	184	$54
Century Communications (15)	705	$110	865	$219	945	$361
E.W. Scripps (19)	-	-	262	$90	702	$260
Post-Newsweek Cable (25)	385	$99	436	$145	482	$186
TCA Cable (26)	338	$60	469	$114	473	$152
Multimedia Cablevision (30)	305	$91	350	$120	417	$165
Total for Group	***18,934***	***$4,975***	***26,373***	***$8,208***	***31,749***	***$11,305***
Industry Totals (average subscribers)	*42,600*	*$11,765*	*51,700*	*$17,855*	*57,400*	*$22,863*
Percentage of Industry Total Accounted for by Group	***44.45%***	***42.29%***	***51.01%***	***45.97%***	***55.31%***	***49.45%***

[4] The fact that the Commission has used the figures for basic subscribers listed in Table 8, does not mean that the Commission has endorsed their use for other purposes. For example, it is likely that several of the cable system operators listed in that table are properly charged with substantially larger numbers of basic subscribers for the purpose of the Commission's attribution rules that are used for determining whether a cable system operator has exceeded the thirty-percent limit imposed by the horizontal ownership rules. *See, e.g., Implementation of Sections 11 & 13 of the 1992 Cable Act: Horizontal & Vertical Ownership Limits, Second Report & Order*, 8 FCC Rcd 8565 (1993).

* Total at end of year. A calculation of revenue or cash flow per subscriber will be somewhat lower when the year-end total number of subscribers is used than when the average numbers of subscribers for the year is used.

** Displayed in descending order according to 1993 total basic subscribers, with the company's rank relative to all systems following in parenthesis.

*** Includes both American Tel. & Communications Corp. (Time, Inc.) and Warner Cable Communications for 1987 and 1990, before the two were completely merged.

**** Includes only Falcon Cable Systems, a division of Falcon Cable TV.

Sources: 1993 Annual Reports for listed companies; PAUL KAGAN ASSOCIATES, INC., THE CABLE TV FINANCIAL DATABOOK 14-15, 37, 62 (1994); PAUL KAGAN ASSOCIATES, INC., THE CABLE TV FINANCIAL DATABOOK 17-18, 41, 66 (1991); PAUL KAGAN ASSOCIATES, INC., THE KAGAN CABLE TV FINANCIAL DATABOOK 20-21, 28-59, 86 (1991); *History of Cable & Pay TV Subscribers & Revenues,* CABLE TV INVESTOR, March 31, 1994, at 9; Tom Kerver, *Cablevision's Top 200,* CABLEVISION, May 23, 1994, at 101-123.

TABLE 9:
Cable Systems Sales Prices

	1987	1990	1993	Pct. Chg. 1987-90	Pct. Chg. 1990-93
Number of Systems Sold	498	105	96	-78.92%	-8.57%
Total Number of Subscribers	6,506,466	531,207	3,852,668	-91.84%	625.27%
Average Size of System (subs.)	*13,065*	*5,059*	*40,132*	-61.28%	693.26%
Number of Homes Passed	11,845,227	870,588	6,628,216	-92.65%	661.35%
Avg. # of Homes Passed	*23,786*	*8,291*	*69,044*	-65.14%	732.73%
Total Dollar Value (billions)	$11.21	$1.07	$8.32	-90.41%	674.48%
Average Dollar Value (million)	*$22.51*	*$10.23*	*$86.69*	-54.53%	747.09%
Value Per Home Passed	*$946*	*$1,277*	*$1,256*	34.95%	-1.67%
Dollar Value Per Subscriber	***$1,723***	***$2,049***	***$2,160***	18.92%	5.43%
Cash Flow Multiple (Ratio of Price to Cash Flow)	***11.7 x***	***11.7 x***	***11.3 x***	***0.00%***	***-3.00%***

Source: *The Year that Disappeared*, CABLE TV INVESTOR, February 24, 1994, at 12; *Mergermania: SW Bell, Cox Tie the Knot*, Cable TV Investor, December 20, 1993, at 6. The Commission excluded transactions that had been reported in 1993, but were not consumated.

TABLE 10:
Cable System Transactions in Principle
That Have Been Announced in 1994

#	Buyer	Seller	System(s)	Mo.	Price (mil.)	Basic Subs.	Price/ Sub.	CF Mult.
1	TCI	Intermedia Partners	Tuscon, AZ	Jan	$250.00	105,000	$2,381	11.9
2	Triax Comm.	Dowden Midwest	Scaumberg, IL	Jan	$0.90	800	$1,125	8.6
3	US Cable Corp.	Panther Valley	Allamuchy, NJ	Jan	$2.50	1,300	$1,923	9.1
4	Charter Comm.	McDonald Invst. Co	AL, GA, LA sys.	Feb	$185.00	100,000	$1,850	10.3
5	Cablevision Ind.	Comm. Sys.	Lexington/Richland, KY	Feb	$6.10	3,000	$2,033	10.8
6	River Valley Cable	Time Warner	Sedona & Flagstaff, AZ	Feb	$33.00	16,300	$2,025	9.9
7	Friendship Cable	Galaxy Cable	AR, LA, TX systems	Feb	$42.60	34,100	$1,249	8.2
8	Marks Cablevision	Chambers	San Bernardino, CA	Feb	$22.50	14,000	$1,607	10.4
9	Marks Cablevision	Simmons Comm.	Ranch. Cucamonga, CA	Feb	$20.00	11,400	$1,754	10.1
10	KBLCOM	Countryside Cable	Bloomington, MN	Mar	$87.00	47,600	$1,828	11.2
11	Falcon Cable TV	Netarts Cable	Netarts, OR	Mar	$1.50	1,300	$1,154	7.8
12	P. Bordes becomes	100% owner of Greater Media		Apr	$225.00	113,400	$1,984	9.3
13	Lenfest Comm.	TCI	Red Lion/Mt. Wolf, PA	Apr	$17.50	10,500	$1,667	9.7
14	Rogers Comm	Maclean Hunter	U.S. systems	Apr.	$1,082.70	494,000	$2,192	11
15	Bresnan	Jones	Gaston Co., NC	Apr	$35.00	19,900	$1,759	9.2
16	Multimedia Cblvsn.	ML Media	Williamston, NC	May	$4.30	3,000	$1,433	10.8
17	Galaxy Mgmt.	Galaxy Cable	IL & KY Systems	May	$18.40	14,900	$1,235	11.8
18	Prestige Cable	Cblvsn/Iredell	Iredell & Alex. Cty, NC	May	$3.40	2,400	$1,417	8
19	Adelphia Comm.	North Star Cable	Fluvanna, VA	May	$2.50	1,400	$1,786	9
20	Adelphia Comm.	Tele-Media Corp.	U.S. systems	May	$345.00	165,000	$2,091	9
21	Cox Cable Comm.	Times Mirror Cable	U.S. Systems	Jun	$2,296.00	1,292,200	$1,777	11
22	Comcast Cable	Rogers Comm.	Maclean Hunter sys.	Jun	$1,270.00	547,000	$2,322	10.5
23	TCI Cblvsn/GA	TCI/ Int. Res.	Baton Rouge. LA	Jun	$191.00	96,500	$1,979	10.5
24	Marcus Ptrs. (14%)	Crown Media	Alabaster, AL	Jun	$12.00	11,000	$1,091	6.2
25	Marcus Ptrs.	Crown Media	WI systems	Jun	$334.00	181,300	$1,842	10.9
26	Charter Comm.	Crown Media	100% of owned & various % of managed	Jun	$554.00	271,000	$2,044	9.4
27	Cblvsn. Systems	Cblvsn. Boston	Boston, MA	Jun	$207.10	130,000	$1,593	9.7
28	US West	Robert Bass Group, including Wometco Cable Corp.	U.S. sys, incl. GA	Jul	$1,200.00	480,000	$2,500	10.8
29	Cblvsn Systems	Nashoba Comm.	Boston, MA. suburbs	Jul	$90.00	34,800	$2,586	n/a
30	Classic Cable	Transwestern	U.S. Systems	Jul	$24.50	20,000	$1,225	9.1
31	TCI	TeleCable Corp.	U.S. Systems	Aug	$1,560.00	740,900	$2,106	10.3
32	Time Warner	Galaxy Cblvsn.	Granada Hills, TX	Aug	$8.00	5,400	$1,481	11.1
33	Comcast	CableSouth	U.S. Systems	Aug	$54.80	28,700	$1,909	9.2
34	Galaxy Telecom.	Vantage	U.S. Systems	Aug	$38.40	30,900	$1,243	7.5
35	Classic Cable	De-Cal Cable	Karnes City, TX	Aug	$3.70	3,500	$1,057	8.6
36	Multimedia	TCI	Wichita, KS area	Aug	$90.00	50,000	$1,800	9
	TCI	Multimedia	Suburbs of Chicago, IL	Aug	$81.00	39,400	$2,056	9.5
37	Cblvsn Systems	Sutton Capital	Monmouth, NJ	Aug	$413.50	177,000	$2,336	n/a
38	Time Warner*	Summit Comm.	Winston-Salem, NC	Sep	$300.00	160,000	$1,875	n/a
	Totals & Weighted Averages **				***$10,950.90***	***5,380,100***	***$2,035***	***10.2***

* The transaction between Time Warner and Newhouse, which was also announced in September, is not included on this list because it involves the creation of a joint venture, and therefore, the Commission was unable to obtain an accurate valuation of the transaction.

** The totals and weighted average sales prices include both transactions involving the Maclean Hunter systems, but only include the differences between the systems involved in the transactions between TCI and Multimedia.

Note: Table 10 includes all transactions that have been identified by the Commission at this time. It is not, however, purported to be a complete list of all transactions that have been announced in 1994.

Sources: *1993 Cable Sales Stats: Telco Buys Bring Them Back to the Future*, CABLE TV INVESTOR, Jan. 28, 1994, at 11; *System Sales: Caught in Credit Crunch III*, CABLE TV INVESTOR, Feb. 28, 1994, at 12; *The Year that Disappeared*, CABLE TV INVESTOR, Feb. 28, 1994, at 12; *Systems for Sale, But Where Are the Buyers?*, CABLE TV INVESTOR, Mar. 31, 1994, at 12; *Deal Tally -- Few & Far Between*, CABLE TV INVESTOR, Apr. 30, 1994, at 8; *Adelphia Taps Into Tele-Media*, CABLE TV INVESTOR, Jun. 7, 1994, at 3; *System Sales Spring to Life*, CABLE TV INVESTOR, Jul. 25, 1994, at 8; *MSOs on the Way Out*, CABLE TV INVESTOR, Aug. 31, 1994, at 6; Mark Robichaux, *Adelphia to Buy 75% Control of Tele-Media*, WALL ST. J., Jun. 8, 1994, at A5; *In Brief*, BROADCASTING & CABLE, Jul. 4, 1994, at 56; Joe Estrella & John M. Higgins, *TCI Swallows TeleCable Corp. in $1.5M [sic.] Deal*, MULTICHANNEL NEWS, Aug. 15, 1994, at 42; John M. Higgins, *Newhouse Deal Sets Stage for New Sales*, MULTICHANNEL NEWS, Sep. 19, 1994, at 1; *A Deal is Completed*, N.Y. TIMES, Aug.9, 1994, at D-17.

APPENDIX D

Date Filed	*Telephone Company*	*Location*	*Homes*	*Type of Proposal*
10/21/92	Bell Atlantic-VA	Arlington, VA	2,000	technical/ market
10/30/92	NYNEX	New York, NY	2,500	technical
11/16/92	New Jersey Bell	Florham Park, NJ	11,700	permanent
12/15/92	New Jersey Bell	Dover Township, NJ	38,000	permanent
04/27/93	Southern New England Telephone	West Hartford, CT	1,600	technical/ market
06/18/93	Rochester Telephone	Rochester, NY	350	technical/ market
06/22/93	US West	Omaha, NE	2,500 or 60,000	technical/ market
12/15/93	Southern New England Telephone (amendment)	Hartford & Stamford, CN	150,000	technical/ market expansion
12/16/93	Bell Atlantic	MD & VA	300,000	permanent
12/20/93	Pacific Bell	Orange Co., CA	210,000	permanent
12/20/93	Pacific Bell	So. San Francisco Bay, CA	490,000	permanent
12/20/93	Pacific Bell	Los Angeles, CA	360,000	permanent
12/20/93	Pacific Bell	San Diego, CA	250,000	permanent
01/10/94	US West	Denver, CO	330,000	permanent
01/24/94	US West	Portland, OR	132,000	permanent
01/24/94	US West	Minneapolis/ St. Paul, MN	292,000	permanent
01/31/94	Ameritech	Detroit, MI	232,000	permanent
01/31/94	Ameritech	Columbus & Cleveland, OH	262,000	permanent
01/31/94	Ameritech	Indianapolis, IN	115,000	permanent
01/31/94	Ameritech	Chicago, IL	501,000	permanent

01/31/94	Ameritech	Milwaukee, WI	146,000	permanent
Date Filed	*Telephone Company*	*Location*	*Homes*	*Type of Proposal*
03/16/94	US West	Boise, ID	90,000	permanent
03/16/94	US West	Salt Lake City, UT	160,000	permanent
04/13/94	Puerto Rico Tel. Co.	Puerto Rico	250	technical
05/23/94	GTE - Contel of Va.	Manassas, VA	90,000	permanent
05/23/94	GTE Florida Inc.	Pinella and Pasco Co., FL	476,000	permanent
05/23/94	GTE California Inc.	Ventura Co., CA	122,000	permanent
05/23/94	GTE Hawaiian Tel. Co.	Honolulu, HA	296,000	permanent
06/16/94	Bell Atlantic (amendment)	Wash. DC LATA	1,200,000	permanent
06/16/94	Bell Atlantic	Baltimore, MD; Northern NJ; DE; Philadelphia, PA; Pittsburgh, PA; and Southeastern VA	2,000,000	permanent
06/27/94	BellSouth	Chamblee & DeKalb Counties, GA	12,000	technical/ market
07/08/94	NYNEX	RI	63,000	permanent
07/08/94	NYNEX	MA	334,000	permanent
09/09/94	Carolina Tel. & Tel. Co.	Wake Forest, NC	1,000	technical/ market

APPENDIX E

MARKET AND TECHNICAL TRIALS, GRANTS AND PENDING APPLICATIONS FOR VIDEO DIALTONE

1. Since the adoption in 1992 of the video dialtone regulatory framework, the Commission has granted five applications for technical and market trials of video dialtone services, and one application for a permanent commercial video dialtone platform. Five additional applications for expanded, new market or technical trials are pending before the Commission, as well as twenty-three applications for permanent commercial authorizations. In this appendix the Commission briefly reviews the status of the trials, grants and pending applications.

A. Technical and Market Trials

2. Bell Atlantic -- Arlington Technical Trial. The first technical trial was granted on March 25, 1993, to Chesapeake and Potomac Telephone of Virginia (now, Bell Atlantic - Virginia) for a one-year technical trial with up to 400 (employee) subscribers in Arlington, Virginia, to test ADSL technology. *See Chesapeake and Potomac Telephone Company of Virginia*, 8 FCC Rcd 2313 (1993). Subsequent to the grant, requests to extend the technical trial into a market trial and to expand the market trial to 2000 subscribers were filed with the Commission. *See Application of Bell Atl. Co. for Section 214 Auth. to Provide VDT Servs. in No. VA.* ("Bell Atl. No. Va. VDT Application"), File No. WPC 6834 (filed Nov. 9, 1993). Special temporary authority ("STA") was granted to allow Bell Atlantic to continue the trial until its application to expand and extend the service is granted, or for six months, whichever occurs first. The STA is due to expire September 25, 1994. The technical feasibility of the service in various network environments is being assessed in the second phase of the trial. Therefore, information on those aspects was not available for review prior to submission of this Report. Program supplier-customers on the Bell Atlantic trial platform in northern Virginia include: HBO, Medstar Communications, Inc., 20th Century Fox, Atrium Group, Inc., Metro-Goldwyn-Mayer Inc., Black Entertainment Television, MTM Entertainment, Inc., Miramar Productions, USA Networks, National Geographic Society Television Division, Multimedia Entertainment, Inc., Worldvision Enterprises, American Medical Television, and Walt Disney Pictures & TV. In its report on the status of its trial, Bell Atlantic reported that no access problems were reported by program supplier-customers. *Six Month Compliance Report of Bell Atl. Co., Bell Atl. No. Va. VDT Application*, File No. WPC-6834 (filed Sep. 23, 1993).

3. NYNEX -- Manhattan Technical Trial. The second technical trial was granted to New York Telephone (NYNEX) on June 29, 1993, for a one-year trial to test an HFC network, video switching technologies and methods for storing and delivering video programming in three multiple-dwelling unit ("MDU") buildings serving 2,500 subscribers in New York City. NYNEX proposed to employ switched and non-switched analog technology initially, and to incorporate digital technology such as asynchronous transfer mode (ATM) switch, compact disk-read only memory (CD-ROM) and digital storage as they became

available. The network configuration involves fiber to a demarcation point within the MDU and coaxial cable drops to connect end-users within the MDU, with initial capacity estimates at 160 channels (the analog switch has 90 output ports and 160 input ports; access to switched video services initially is limited to 50 end-users). *Application of New York Telephone Co. for Section 214 Auth. to Provide VDT Servs. in New York City ("NYNEX New York VDT Application")*, 8 FCC Rcd 4325 (1993). NYNEX submitted the required report to the FCC on the status of the trial on July 15, 1994. *Six Month Compliance Report of NYNEX, NYNEX New York VDT Application*, File No. WPC 6836 (filed July 15, 1994). NYNEX reports spirited competition between its customer-programmers, particularly between Liberty Cable and Time Warner Cable. NYNEX is providing end-users a choice between two cable or direct-access programmer customers, Liberty Cable and Time Warner Cable, with a select number of end-users having access to on-demand programming from several information providers, including Liberty Cable, Time Warner, and Urban Communications Transport Corp. The programmer-customers participating in the stored access aspect of the trial include Capital Cities/ABC Video Entertainment, Educational Broadcasting Station WNET, Lincoln Center, Reuters, Archive Holdings, Advanced Research and Technology, Liberty Cable and Television, and Urban Transport. The NYNEX trial is being conducted in two phases. The first phase utilizes an analog system. The second phase of the trial, originally scheduled to begin in the fourth quarter of 1994, proposes to test a digital interactive system, while continuing to provide basic analog transport services. NYNEX reports a postponement in deployment of the digital phase of the trial due to delays in the availability of equipment. *Id.*

4. SNET -- West Hartford Technical and Market Trial. Southern New England Telephone Company (SNET) was granted a one-year authorization on November 12, 1993, for a technical and market trial to serve between 200 and 1600 customers in West Hartford, Connecticut and to test FTTN architecture with coaxial facilities from the node to individual subscribers. *Application of Southern New England Telephone Co. for Section 214 Auth. to Provide CDT Servs. in West Hartford, Conn. ("SNET West Hartford VDT Application")*, 9 FCC Rcd 1019 (1993). The system proposes to provide 110 channels of video initially, with possible expansion to approximately 500 channels using digital compression. In addition to delivering multichannel and single channel video, the network is intended to be capable of delivering to subscribers on-demand movies and other advanced interactive services, such as home shopping, educational and health care services. SNET is authorized to test enhanced and non-common carrier services such as digitizing, compressing, sorting video programming, operating a video switch and the provision of video customer premises equipment, in addition to testing customer interest in menu access and video-on-demand services. SNET also proposes to charge subscribers for the service to test interest and willingness to pay for services available from the video dialtone platform. *Id.* Shortly after grant of the technical and market trial, SNET requested an authorization to expand the trial to pass 150,000 homes. *Request for Expansion of Serv., SNET West Hartford VDT Application*, File No. WPC 6858 (filed Dec. 15, 1993).

5. U.S. West -- Omaha Technical and Market Trial. On December 22, 1993, U.S. West was granted an authorization for technical and market trials in Omaha, Nebraska. The technical trial will be for six months and may pass either 2,500 or 10,000 homes, depending on whether or not U.S. West files a tariff for the service. The market trial will be for the twelve months following the technical trial and may pass up to 60,000 homes. U.S. West will construct an advanced fiber-to-the-curb/coaxial cable network capable of providing 77 channels of analog video and between 800 and 1000 channels of digital capacity. *See Application of US West Communications, Inc. for Section 214 Auth. to Provide VDT Servs. in Omaha, Neb.*, 9 FCC Rcd 184 (1993). U.S. West predicted that approximately fifteen percent of the homes passed would elect to participate in the trial. The grant was also conditioned on US West charging tariffed rates if the service passed more than 2500 homes. The architecture consists of a hybrid fiber-to-the-curb/coaxial cable network for video dialtone, voice and data service, with the components including a gateway that combines and distributes signals from video providers, fiber optic cables, video nodes that convert optical signals to electrical signals, coaxial cable distribution system and interdiction devices that provide network control and end user access to individual analog channels. *Id.*

6. Rochester Telephone Co. -- Rochester Technical Trial. The fifth authorized trial was granted on March 25, 1994 to Rochester Telephone Co., for six months to conduct a tariffed field test to serve up to 120 subscribers using two architectures: a fiber-coax system within multi-unit and single-unit dwellings, and an ADSL system utilizing Discrete Multi-Tone technology within a defined two mile area. *See Application of Rochester Tel. Corp. for Section 214 Auth. to Provide VDT Servs. in Rochester N.Y.*, 9 FCC Rcd 2285 (1994). Rochester Telephone filed a tariff prior to commencement of its trial because it intends to charge both programmer-customers (the video information providers) and subscribers (end-users) for its video dialtone service. Rochester Telephone Corporation, Tariff FCC No. 3, Transmittal No. 224, filed May 17, 1994. Rochester states that it will construct, operate, own and maintain the facilities necessary to transport the video dialtone service, and the programmer-customer will supply, operate, and own the setup box and be responsible for providing all content and programming and service to the subscriber. Rochester's tariff indicates that the HFC network will provide programmer-customers 6-MHz channels and an interactive (4-MHz downstream and 40-KHz upstream) channel per specific customer location. The ADSL system will provide programmer-customers 6-MHz channels and an interactive (6-Mbps downstream and 16-Kbps upstream) channel per specific customer location. Rochester Telephone is testing the capabilities of the ADSL system to transmit a compressed digital video signal over embedded cooper loop plant in order to offer video dialtone service to customers located in areas where fiber optic and coaxial cable facilities have not been deployed. Rochester Telephone Corporation, Tariff FCC No. 3, Transmittal No. 224, filed May 17, 1994.

7. Additional Applications for Initial Trial. Three additional applications for initial trials are pending before the Commission. Puerto Rico Telephone Company has requested a one-year technical trial authorization to serve 250 homes using FTTC and 18 schools and 12 business offices using ADSL network architecture. *See Application of Puerto Rico Telephone Co.*, File No. WPC-6949 (filed April 13, 1994). The trial proposes initial

deployment of 64 analog video channels over the FTTC system, with future enhancement through digital compression to 384 channels.

8. BellSouth proposes an eighteen-month trial to pass 12,000 homes in DeKalb County and Chamblee, Georgia for the purpose of testing an HFC network offering both traditional channel service with 60 analog channels and a digital video dialtone platform with approximately 300 channels utilizing both digital multi-cast and digital point-cast. *See BellSouth Application*, File No. WPC-6977 (filed June 27, 1994). Digital multi-cast entails distribution of a digital video signal to everyone who subscribes, while digital point-cast is switched digital distribution.

9. Carolina Telephone and Telegraph Company has requested authorization for a two-year technical and market trial to 1000 homes in Wake Forest, North Carolina. *See Application of Carolina Telephone and Telegraph Co.*, File No. WPC-6999 (filed Sep. 9, 1994)

10. Trial Cost Estimates. The cost estimates for the various trials are as follows: C&P of Virginia, 400 end-user subscribers at a cost of less than $5 million; NYNEX, 2500 potential end user-subscribers at a cost of less than $3 million; SNET, 1600 potential end user-subscribers at a cost of less than $3 million; US West, 2500 potential end user subscribers at a cost of less than $8.4 million. *US West Communications, Inc.*, 9 FCC Rcd at 188 n. 59. The trial proposed by Bell Atlantic for 2000 households in Virginia is estimated to cost over $11 million. *Id.* The Puerto Rico trial is estimated to cost approximately $2.5 million.

B. Applications for Permanent Commercial Service

11. Twenty-four applications for permanent commercial video dialtone services have been filed with the Commission, including applications by six of the seven RBOCs, as well as GTE. Pacific Bell has filed applications for permanent authority to serve 210,000 homes in Orange County, 490,000 homes in San Francisco, 360,000 homes in Los Angeles and 250,000 homes in San Diego, CA. *See* File Nos. WPC-6913 to WPC-6916, filed December 20, 1993. U.S. West has requested permanent authorizations to serve 330,000 homes in Denver, CO, 132,000 homes in Portland, OR, 292,000 homes in Minneapolis-St.Paul, MN, 90,000 homes in Boise, ID, and 160,000 homes in Salt Lake City, UT. *See* File No. WPC-6919 filed January 10, 1994, File Nos. WPC-6921and WPC-6922, filed January 24, 1994, and File Nos. WPC-6944 and WPC-6945, filed March 16, 1994. Ameritech has requested permanent authorizations to serve 232,000 homes in Detroit, MI, 262,000 homes in Columbus and Cleveland, OH, 115,000 homes in Indianapolis, IN, 501,000 homes in Chicago, IL, and 146,000 homes in Milwaukee, WI. *See* File Nos. WPC-6926 to WPC-6930 filed January 31, 1994. GTE has requested permanent authorizations to serve 90,000 homes in Virginia, 476,000 homes in Florida, 122,000 homes in California and 296,000 homes in Hawaii. *See* File Nos. WPC-6955 to WPC-6958 filed May 23, 1994. Bell Atlantic has requested permanent authorizations to serve 1.2 million homes in the Washington DC metropolitan area and 2 million in the Baltimore-New Jersey-Philadelphia-Pittsburgh

area. *See* File No. WPC-6912 as amended June 16, 1994, and File No. WPC-6966 filed June 16, 1994. NYNEX has requested permanent authorizations to serve 63,000 homes in portions of Rhode Island and 334,000 homes in portions of Massachusetts. *See* File Nos. WPC-6982 and WPC-6983 filed July 8, 1994 and supplemented on July 29, 1994.

12. The first permanent commercial video dialtone authorization was recently granted to New Jersey Bell for Dover Township. *New Jersey Bell Telephone Co.*, 9 FCC Rcd 3677 (1994), *pets. for recon. and mots. for stay pending*, File No. WRC-6840, and *appeals pending, Apelphia Communications, Inc. v. FCC*, No. 94-1616 (D.C. Cir., Sept. 7, 1994). Pursuant to that grant, New Jersey Bell is authorized to construct and operate a video dialtone system to provide video dialtone service to approximately 38,000 homes using a FTTC architecture, with coaxial cable and copper wire for the final link to the home and providing initial digital capacity of 64 channels, conditioned upon expanding capacity to 384 digital channels in January of 1995. *Id.*, 9 FCC Rcd at 3678. New Jersey Bell predicts that 35% of the homes passed will become end-user subscribers. *Id.*

APPENDIX F

Description of Program Access Cases Resolved (as of September 19, 1994)

1. *Petition of Time Warner Cable for Exclusivity*, 9 FCC Rcd 3221 (1994). Time Warner Cable filed a petition for exclusivity requesting authority to enforce, for a period of fifteen years, an exclusive distribution agreement with Courtroom Television (Court TV), a cable programming network. Liberty Cable, a SMATV operator, opposed the petition. On June 1, 1994, the Commission denied Time Warner's request. The Commission ruled that: (1) denial of access to Court TV to competitors will adversely affect competition in the local distribution market, because of its impact on Liberty's ability to compete in Manhattan and New York City, and could similarly limit the development of competition in other local distribution markets and in the national market; (2) Time Warner failed to show that exclusivity is necessary to either (a) attract capital investments for production, promotion, distribution, or carriage of Court TV, which is an established cable network with a growing subscriber base, or (b) promote diversity in programming; and (3) Time Warner would not be able to demonstrate that fifteen years is necessary, in any event, to justify exclusivity.

2. *Petition of New England Cable News for Exclusivity*, 9 FCC Rcd 3231 (1994). New England Cable News, a new regional cable news network, requested a public interest determination that would allow it to enter into exclusive program distribution agreements with cable system affiliates. The petition was unopposed. On June 1, the Commission granted the petition on the following grounds: (1) the ability to offer exclusivity to cable affiliates is necessary to attract investment and secure distribution essential to the financial viability of NECN; (2) NECN's ability to offer exclusive distribution rights to cable affiliates will foster diversity in the programming market; and (3) the public interest benefits of reasonably tailored exclusivity offset any detrimental effect exclusivity has on competition in the New England market. The Commission limited the exclusivity that NECN may offer to exclusive distribution for eighteen months to cable affiliates in the six New England states identified.

3. *Consumer Satellite Systems, Inc. v. Lifetime Television*, 9 FCC Rcd 3212 (1994). Consumer Satellite Systems ("CSS") filed a complaint against Lifetime Television, alleging excessive and discriminatory pricing for Lifetime's programming service. Subsequently, CSS requested dismissal of its complaint, because Lifetime had restructured its ownership so that it was no longer a vertically-integrated vendor. The parties also settled issues relating to pricing practices during the time that Lifetime was still subject to the rules. On June 24, the Cable Services Bureau dismissed the complaint, as not falling under the Commission's rules.

4. *Mid-Atlantic Cable Service Co. v. Home Team Sports and Columbia Cable of Virginia*, 9 FCC Rcd 3991 (1994). In June, 1994, the parties settled this complaint, which involved allegations of exclusivity, unfair practices and discrimination, including predatory pricing and undue influence. Both Mid-Atlantic and Columbia Cable serve Prince William County. Mid-Atlantic alleged it could not buy the Home Team Sports channel, but that

Columbia could, because of Columbia's TCI affiliation. Although there was no exclusive HTS/Columbia contract, Mid-Atlantic alleged *de facto* exclusivity growing from and related to the other alleged unfair and discriminatory practices. Pursuant to the settlement agreement, the Cable Services Bureau dismissed Mid-Atlantic's complaint with prejudice.

5. *Liberty Cable Company, Inc. v. Courtroom Television Network*, 9 FCC Rcd 4035 (1994). Liberty Cable Company, a SMATV operator in New York City, alleged that Court TV had violated the program access rules by refusing to provide its programming to Liberty, based on an exclusive agreement with Time Warner Cable. Prior to the filing of this complaint, Time Warner had filed a petition for exclusivity with respect to its contracts with Court TV and Prime Ticket Network. On March 25, 1994, the Bureau held Liberty Cable's complaint against Court TV in abeyance pending the outcome of Time Warner's petition for exclusivity. *See Complaint of Liberty Cable Co., Inc. v. Courtroom Television Network*, 9 FCC Rcd 2324 (1994). On June 1, 1994, the Commission denied Time Warner's exclusivity petition. *Time Warner Cable*, 9 FCC Rcd 3221 (1994). The Bureau determined that under the terms of the Commission's Order, Court TV could not refuse to distribute its programming to Liberty or any other MVPD, on the basis of its exclusive distribution agreement with Time Warner. Accordingly, the Bureau dismissed Liberty's complaint as moot, but without prejudice to refile if subsequent negotiations gave rise to a new program access complaint.

6. *Petition for Exclusivity of Time Warner Cable*, 9 FCC Rcd 4029 (1994). Time Warner Cable filed a petition for exclusivity requesting the authority to enforce an exclusive distribution agreement with Prime Ticket Network in ten communities in southern California. Vanguard Communications, Inc., a SMATV and MMDS operator, and the California Attorney General opposed the petition. Time Warner Cable withdrew its petition and stated that it will not enforce the exclusive provisions of the distribution agreement. Vanguard requested that the Commission condition withdrawal and dismissal of the petition on Time Warner's amendment of the distribution agreement with Prime Ticket. The Bureau determined that such conditions were unnecessary because without a public interest determination from the Commission such exclusive distribution agreements are unenforceable. On August 1, 1994, the Cable Services Bureau dismissed the petition.

7. *Petition of Walt Disney Company for Waiver of Program Access Rules*, 9 FCC Rcd 4007 (1994). Disney requested a waiver of the program access rules so its subsidiary, The Disney Channel, would not be considered a vertically integrated programming vendor by virtue of Disney's operation (through a subsidiary, Madeira Land Company) of a cable system serving almost exclusively the Disney World hotels. The hotels receive the channel from the Madeira system and then distribute it to guest rooms using internal wiring. Disney claimed that Madeira's few subscribers -- the hotels -- constituted less than 1/1000th of one percent of The Disney Channel's subscribers, and that Madeira's monthly license fee for the channel accounted for less than 1/40th of one percent of the channel's revenues. Disney argued that its interests as a cable operator were so *de minimis* that it lacked any incentive to refuse to sell programming to a competing distribution system or discriminate against competing systems by charging higher rates for the programming or imposing other

discriminatory conditions. The Bureau granted a conditional waiver, based on the fact that Madeira, although technically a cable system, is not the kind of distribution system the program access rules were designed to reach, and because the Disney Channel is widely available. The Bureau conditioned the waiver on Disney's reappearance before the Commission to have the waiver continue in force if Madeira either begins residential distribution or adds other non-Disney hotels to its distribution system.

8. *Electric Plant Board, City of Glasgow, KY v. Turner Network Cable Sales, Inc.*, DA 94-974, (CSR-4188-P, released September 6, 1994). Glasgow's municipal utility and electricity board, an overbuilder, alleged that its competitor, Telescripps Cable Company, was illegally enforcing an exclusive programming distribution contract with Turner to distribute TNT. Because this is an "area served by a cable operator," this type of contract is not prohibited *per se*, but Glasgow alleged that the parties cannot enforce it without first obtaining a favorable public interest determination from the Commission. Turner claimed the contract was grandfathered, as it was entered into before June 1, 1990. Glasgow claimed that a new contract was made when the contract was modified and extended in August, 1990. The Bureau dismissed Glasgow's complaint because it determined that the contract was grandfathered under the 1992 Cable Act. The Bureau noted in its dismissal that the exclusive contract was scheduled to expire October 31, 1994 and at that time Turner would be obligated to negotiate with Glasgow or to petition the Commission for a public interest determination.

9. *Hutchens Communications Inc. v. TCI Southeast and TCI of Georgia*, DA 94-975 (CSR-4230-P, released September 6, 1994). Hutchens, the owner and operator of a video production company, created and produced The Welcome Channel (TWC), that was carried by TCI initially without a lease fee. In 1993, TCI took the position that TWC was a leased access channel under the Commission's new rules and that a monthly lease was now warranted. Hutchens and TCI could not agree on the amount of the fee and TCI terminated carriage. Hutchens claimed that the fee was not justified under the leased access rules and was an unfair practice under the program access rules. Hutchens also claimed that TCI engaged in other unfair practices, including calling Falcon Cable (another cable system in the area that carries TWC) to encourage it to terminate TWC. TCI contended the fee was justified under the leased access rules, and that Hutchens' program access theory was misplaced, as Hutchens is not an MVPD. TCI also disputed Hutchens' other claims of unfair practices and claimed that the complaint was not properly verified and was untimely under the leased access rules. The Bureau dismissed the complaint on the grounds that the leased access claim was untimely filed and that Hutchens lacked standing to bring a program access complaint because it did not fall within the statutory definition of a multichannel video programming distributor.

10. *CableAmerica v. Times Mirror*, DA 94-985 (CSR-4024-P, released Sep. 9, 1994). CableAmerica, a 9,000 subscriber MVPD in Mesa, Arizona, competes directly with Dimension Cable Services, a subsidiary of Times Mirror Cable Television, Inc., with approximately 40-50,000 subscribers. According to CableAmerica, Times Mirror owns the Arizona Sports Programming Network, which carries professional and other live sporting

events featuring teams based in Arizona or otherwise of interest to Arizona residents. CableAmerica filed a complaint in January 1993. In February 1993, the Cable Television Branch sent CableAmerica a letter stating that the complaint was premature and that it would not be accepted for filing at this time because the Commission had not yet adopted its program access rules. CableAmerica filed a petition for reconsideration of this decision, which remained pending. CableAmerica refiled its complaint on August 10, 1993 alleging that ASPN refused to sell its programming to CableAmerica's Mesa system. Pursuant to a negotiated settlement agreed to by the parties, the Bureau dismissed the complaint.

11. *Private Network Cable Systems Company v. SportsChannel New York,* File No. CSR-4233-P. Private Network Cable Systems Company ("PNC") is a multichannel video programming distributor operating satellite master antenna television systems in two multi-unit housing complexes in Queens, New York. SportsChannel is a vertically integrated programmer who offers its programming to Time Warner, a direct competitor of PNC. PNC alleged that SportsChannel was discriminating against PNC vis-a-vis Time Warner in the pricing of programming. PNC recently filed a request to withdraw its complaint, with prejudice, because the parties have reached an amicable settlement. An order dismissing the case will be released shortly.

APPENDIX G

TABLE 1
1994 HORIZONTAL CONCENTRATION IN THE CABLE TELEVISION INDUSTRY[1]

Rank	Company	Total Industry[2]
1	TCI	24.75%
2	Time Warner	12.53
3	Continental Cablevision	5.08
4	Comcast	4.82
Top 4		*47.18*
5	Cablevision Systems	3.78
6	Cox Cable	3.12
7	Newhouse	2.41
8	Cablevision Industries	2.33
Top 8		*58.81*
9	Jones Spacelink	2.24
10	Times Mirror	2.23
Top 10		*63.29*
Top 25		*83.41*
Top 50		*92.42*
HHI		***898.00***[3]

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[1] Data as of March 31, 1994. *Top 100 Cable System Operators as of March 31, 1994,* CABLE TV INVESTOR, June 7, 1994, at 17.

[2] Percentage based on share of total industry subscribers for 1994, which was calculated to be 57,900,000 by estimating from year-end 1993 total, and assuming continuation of the 1990-93 industry trend for total subscriber growth. PAUL KAGAN ASSOCIATES, INC., CABLE TV FINANCIAL DATABOOK 7 (1994).

[3] The HHI is calculated on the basis of the top 50 companies' shares of the total subscribers in the industry. If data were available for all other companies in the industry, the number could increase no more than 2.1 points to a total of 900.

TABLE 1A
HORIZONTAL CONCENTRATION AFTER
1994 MERGERS IN THE CABLE TELEVISION INDUSTRY[1]

Rank	Company	Share of Total Industry[2]
1	TCI	26.01%
2	Time Warner	15.21
3	Comcast	5.57
4	Cox Cable	5.35
Top 4		*52.14*
5	Continental Cablevision	5.08
6	Cablevision Systems	3.78
7	Cablevision Industries	2.33
8	Jones Spacelink	2.24
Top 8		*65.57*
9	Adelphia	2.17
10	Viacom	1.90
Top 10		*69.64*
Top 25		*87.35*
Top 50		*95.16*
HHI		***1051.00***[3]

This table takes account of the effects of the following proposed transactions: (1) TCI's acquisition of Telecable; (2) Comcast's acquisition of Maclean Hunter systems in the United States; (3) Cox's acquisition of Times Mirror; and (4) Time Warner's joint venture with Newhouse.

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[1] Data as of March 31, 1994. *Top 100 Cable System Operators as of March 31, 1994,* CABLE TV INVESTOR, June 7, 1994, at 17.

[2] Percentage based on share of total industry subscribers for 1994, which was calculated to be 57,900,000 by estimating from year-end 1993 total, and assuming continuation of the 1990-93 industry trend for total subscriber growth. PAUL KAGAN ASSOCIATES, INC., CABLE TV FINANCIAL DATABOOK 7 (1994).

[3] The HHI is calculated on the basis of the top 50 companies' shares of the total subscribers in the industry. If data were available for all other companies in the industry, the number could increase no more than 2.1 points to a total of 1053.

TABLE 2
CHANGES IN CONCENTRATION OF CONTROL OF THE CABLE INDUSTRY BASED ON TOTAL SUBSCRIBERS

	1989	1990	1991	1992	1993	1994	POST 1994 MERGERS
Top Co. Share	24.4	24.0	24.5	25.2	24.3	24.8	26.0
Top 4 Share	45.8	46.9	46.0	48.1	47.2	47.2	52.1
Top 8 Share	57.3	58.7	57.2	60.0	58.7	58.8	65.6
Top 10 Share	61.7	62.9	61.4	64.4	63.2	63.3	69.6
Top 25 Share	80.7	82.1	80.2	84.3	83.1	83.4	87.4
Top 50 Share	91.6	93.5	90.9	95.0	93.1	94.4	95.2
HHI	***867.00***	***866.00***	***872.00***	***928.00***	***880.00***	***898.00***	***1051.00***

Sources: Data for 1994 and Post-Merger taken from Appendix G, Table I & Table IA. Data for 1989 through 1994 was calculated from information appearing in PAUL KAGAN ASSOCS., INC., CABLE TV FINANCIAL DATABOOK 16 (1990); PAUL KAGAN ASSOCS., INC., CABLE TV FINANCIAL DATABOOK 14 (1991); PAUL KAGAN ASSOCS., INC., CABLE TV FINANCIAL DATABOOK 12 (1992); PAUL KAGAN ASSOCS., INC., CABLE TV INVESTOR 12 (1993); PAUL KAGAN ASSOCS., INC., CABLE TV FINANCIAL DATABOOK 12 (1994). Data for 1994 was calculated from information appearing in CABLE TV INVESTOR, June 7, 1994, at 17. Total subscriber information was calculated from CABLE TV INVESTOR, March 31, 1994 at 9. The figure for total industry subscribers for 1994 is estimated by begining with year-end 1993 total and assuming continuation of the industry trend for total subscribers 1990-93. Data for 1991-94 have been recalculated after discussions with Paul Kagan Associates personnel about consolidated, non-consolidated and international subscribers. International subscribers for TCI are deducted from its total subscribers for 1991-93; estimates for 1994 assume continuation of historical trends. TCI data for 1990 was calculated from its last year-end filing with the Securities and Exchange Commission. Tele-Communications, Inc., Form 10K I-2, I-4 (Dec. 31, 1993).

Table 3

National Programming Services With Ownership Interests Held by Cable Operators

Programming Services	*Launch Date*
Action Pay Per View	Sep-90
All News Channel	Nov-89
American Movie Classics	Oct-84
Black Entertainment Television	Jan-80
Bravo	Feb-80
C-Span I	Mar-79
C-Span II	Jun-86
Cable Health Club	Oct-93
Cable News Network	Jun-80
Cartoon Network	Oct-92
Cinemax	Aug-80
Comedy Central	Apr-91
Country Music Television	Mar-83
Court TV	Jul-91
Discovery	Jun-85
E! (formerly Movietime)	Jul-87
Encore	Apr-91
Family	Apr-77
Flix!	Apr-91
GEMS Television	Apr-93
HBO	Dec-75
Headline News	Jan-82
Home Shopping Network I	Jul-85
Home Shopping Network II	Sep-86
International Channel	Jul-90
KTVT Dallas	Jul-84
Mind Extension Univeristy	Nov-87
The Movie Channel	Dec-79
MTV Latino	Oct-93
MTV: Music Television	Aug-81
NewSport	Feb-94
NICK at Nite	Jul-85
Nickelodeon	Apr-79
Prime SportsChannel Network	Jan-89
QVC	Nov-86
QVC Fashion Channel	Dec-91

Table 3

Request 3-5	Sep-93
Request Television	Nov-85
Request Television 2	Jul-88
Sci-Fi Channel	Sep-92
Showtime	Jul-76
TBS Atlanta	Dec-76
Television Food Network	Nov-93
The Box	Dec-85
The Learning Channel	Nov-80
The Nashville Network	Mar-83
Turner Classic Movies	Apr-94
Turner Network Television	Oct-88
USA Network	Sep-80
VH-1	Jan-85
Viewers Choice 1	Nov-85
Viewers Choice 2: Hot Choice	Jun-86
Viewers Choice Continuous Hits 1	Feb-93
Viewers Choice Continuous Hits 2,3	Aug-93
Viva Television Network	Jan-93
Z Music	Mar-93

This table was derived from a study prepared by Economists, Inc., submitted with NCTA Comments and was updated to reflect recent launches and information. *See* NCTA Comments, Attachment C, Table 1; Liberty Media Comments at 9; *Cable Network Ownership,* Cable TV Programming, Aug. 29, 1994.

Table 4

National Programming Services Without A Cable Operator Holding An Ownership Interest

Programming Service	*Launch Date*
Adam & Eve Channel	Feb-94
Alternate View Network	Oct-85
Network	Feb-84
America's Talking	Jul-94
Americana Television	Apr-94
Arts & Entertainment	Feb-84
Cable Video Store	Jan-85
Caribbean Satellite Network	Dec-92
CNBC	Apr-89
The Crime Channel	Jul-93
Deep Dish TV Network	Jan-86
Disney Channel	Apr-83
Employment Channel	Feb-92
ESPN	Sep-79
ESPN2	Oct-93
EWTN	Aug-81
Faith and Value Network (formerly VISN/ACTS)	May-84
Foxnet	Jul-91
fX	Jun-94
Galavision/ ECO	Oct-79
Hit Video USA	Dec-85
The Inspirational Network	Apr-78
Jewish Television Network	Jan-81
KTLA	Mar-88
Lifetime	Feb-84
Mor Music TV	Aug-92
NASA Television	Jul-91
National Empowerment Television	Dec-93
National Jewish Television	May-81
The 90s Channel	Nov-89
Nostalgia Channel	Feb-85
Playboy Channel	Nov-82
Prevue Channel	Jan-88
SCOLA	Aug-87

Table 4

Spice	May-89
Spice 2	Feb-94
Telemundo	Jan-87
Theatre Vision	May-93
The Travel Channel	Feb-87
Trinity Broadcasting Network	Apr-78
TV-Japan	Jul-91
U Network	Oct-89
Univision	Sep-76
ValueVision	Oct-91
The Weather Channel	May-82
WGN	Nov-78
Worship	Sep-92
WPIX	May-84
WSBK	Feb-88
WWOR	Apr-79

This table was derived from a study prepared by Economists, Inc. for the NCTA and was updated to reflect recent launches before July 30, 1994. NCTA Comments, Attachment C, Table 2; *America's Talking: High Hopes*, Cable TV Programming, July 25, 1994, at 2; *Cable Network Ownership*, Cable TV Programming, Aug. 29, 1994 .

Table 5

Announced National Launches of Programming Services For Cable Distribution

Programming Services Without a Cable Operator Holding An Ownership Interest

Action America
Applause
Arts & Antique Network
ATV
Auto Channel
Automotive Television Network
Booknet
Canal de Noticias/NBC
Career & Education Opportunity Network
CEO Channel
Collectors Channel
Cupid Network Television
Ecology Channel
Enrichment Channel
ESPN 3
Fashion & Design Channel
Filipino Channel
Fitness & Interactive Television
Game Show Channel
Gaming Entertainment Television
Global Mind Network
Global Village Network
Golden American Network
Golf Channel, The
Health & Fitness Channel
Health Channel
History Channel
History Network
Hobby Craft Network
Home Interactive TV
Horizons Cable
Idea Channel, The
Independent Film Channel

The Interactive Channel
Military Channel
MOR/Aerobic Music
MOR/Classic Country
MOR/Classic Rock
MOR/Concert Music
MOR/Gospel Music
MOR/Spanish Music
National & International Singles Television Network
National Access
Network 1
New Culture Network
Ole TV
Our World Television
Ovation
Parent Television
Parenting Satellite TV Network
Parents Channel
Planet Central Television
Popcorn Channel
Recoverynet/ The Wellness Channel
S The Shopping Network
Sewing & Needles Arts Network
Single Information News Network
SingleVision
Sports Recreation News
Talk Channel
Talk TV Network
Telenoticias
TFN: The Fashion Network
Therapy Channel
TRAX
TV Macy's
World African Network
XTV

Table 5

Programming Services With Ownership Interests Held by Cable Operators

BET Jazz
Catalog 1
Classic Sports Network
CNN International
Encore/Action
Encore/Love Stories
Encore/Mystery
Encore/True Stories
Encore/Tweens
Encore/Westerns
Game Net
Home & Garden TV
Jones Computer Network
Jones Health Care Channel
Jones Language Network
La Candena Deportiva
Music Video Store
Outdoor Life Channel
Product Information Network
Q2/On Q
Romance Classics
Sega Channel
Showtime Comedy Television
Showtime Family Television
Showtime Film Festival
Showtime/Action
Starz!
TCI/Bertelsmann channel
TCI/Microsoft PC Channel
Television Shopping Mall

Sources: *A Who's Who of New Nets*, Cablevision, May 9, 1994, at 35A-45A; *Database*, Cablevision, June 6, 1994, at 54.

Table 6

Table 6

Major MSO Ownership in National Programming Services

Services	Cablevision	Comcast	Continental	Cox	Jones	Newhouse	TCI 1/	Times Mirror	Time Warner	Viacom
Action Pay-Per-View 2/							21.40%		17.70%	
All News Channel 3/										100.00%
AMC	75.00%									
BET							21.40%		17.70%	
The Box 1/						4/	7.00%			
Bravo	50.00%									
Cable Health Club							18.00%			
Cartoon 5/	x		x		x		23.30%	x	19.50%	
Cinemax									100.00%	
CNN 5/	x		x		x		23.30%	x	19.50%	
Comedy Central									50.00%	50.00%
Court TV	16.70%						33.00%		33.00%	
Discovery				24.00%		24.00%	49.00%			
E!		10.30%	10.30%	10.30%		10.30%	10.30%		48.30%	
Encore							90.00%			
FAM							18.10%			
Flix!										100.00%
HBO									100.00%	
Headline News 5/	x		x		x		23.30%	x	19.50%	
HSN							80.00%			
HSN II							80.00%			
Learning Channel				24.00%		24.00%	49.00%			
Mind Ext. Univ.					100.00%					
Movie Channel										100.00%
MTV										100.00%
MTV Latino 3/										100.00%
Newsport 6/	25.00%						38.00%			
Nick at Nite 3/										100.00%
Nickelodeon										100.00%
Prime SportsChannel 7/	25.00%						38.00%			

Services	Cablevision	Comcast	Continental	Cox	Jones	Newhouse	TCI 1/	Times Mirror	TW	Viacom
QVC 8/	x	16.40%	x			x	28.20%	x	10.70%	
QVC Fashion 8/	x	16.40%	x			x	28.20%	x	10.70%	
Request Television							9/			
Sci-Fi Channel										50.00%
Showtime										100.00%
TBS 5/	x		x		x		23.30%	x	19.50%	
Television Food Network			10/					10/		
TNT 5/	x		x		x		23.30%	x	19.50%	
Turner Movie Classic 5/	x		x		x		23.30%	x	19.50%	
USA										50.00%
VH-1										100.00%
Viewers Choice 11/		11.00%	12.00%	13.00%		11.00%		x	17.00%	11.00%

Unless otherwise noted, the source for all figures is *Cable Network Ownership,* Cable TV Programming, August 29, 1994, at 2-3. Ownership interests reported for earlier periods may not reflect current ownership. Includes both direct and indirect ownership interests.

1/ Liberty Media's interests are consigned to TCI. As of June 1994, Liberty Media reported its interests in BET as 18%, in The Box as 7%, in Family and Cable Health Club as 18% and in QVC as 18.5%. Liberty Media Comments at 9.

2/ A programming service of BET Holdings, Inc. *See* BET Holdings, Inc., 1993 Annual Report at 4.

3/ *See* Viacom Reply Comments at 1-2.

4/ As of May 24, 1993, Newhouse reportedly held a 17% interest in The Box. *See* John M. Higgins, Bailout of Video Jukebox Network Crumbling, Multichannel News, May 24, 1993, at 57.

5/ A programming service of Turner Broadcasting System. Interests marked by an "x" are less than 5% and together with smaller MSOs represent 32.8% ownership in TBS. *See* NCTA Comments, Attachment C, Table 4.

6/ As of September 1993. *See* Rachel Thompson, CBS Dumps Public Affairs Network, Multichannel News, Sept. 27, 1993, at 2.

7/ As of January 1993. *See* Rich Brown, Prime Network, SportsChannel to Merge, Broadcasting January 11, 1993, at 4.

8/ All cable operators' interests less than 5%, marked by an "x," total 42% as of July 1993. *See Cable Network Ownership,* Cable TV Programming, July 30, 1993, at 6-7. Comcast and Liberty Media have reportedly created a partnership to hold QVC interests, through which Comcast would own 57.56% and Liberty would own 42.44% of QVC. Cable TV Programming, July 25, 1994, at 1.

9/ TCI's ownership in Request Television is unknown. However, as of April 1992, TCI together with News Corp. reportedly acquired a majority interest in the owner of Request Television, Reiss Media. *See* Sharon Moshavi, *TCI, News Corp Buy Stake in Reiss,* Broadcasting, April 6, 1992, at 11.

10/ Actual ownership percentages in TV Food Network are unknown, though Continental is reported to be a "primary owner" and Times Mirror a "minority owner." In addition to Times Mirror and Continental the following cable operators reportedly hold ownership interests in the Television Food Network: Scripps Howard (primary), Adelphia (minority) and CVI (minority). *Cable Network Ownership,* Cable TV Programming, Aug. 29, 1994, at 3.

11/ As of September 1993. *See* David H. Waterman & Andrew A. Weiss, *Vertical Integration in Cable Television,* Table 2-2, September 17, 1993. Cox's current ownership interest is reported as 20%. *See Cox /Times Mirror Deal Emphasizes Content,* Cable TV Programming, June 23, 1994, at 3.

Table 7

Vertical Connection Between Major Programming Services and Cable System Operators

Programming Network (Top 25)	Subscribers (millions)	MSO with Ownership Interest in Network	Launch Date
ESPN	61.8	None	Sep-79
CNN	61.6	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR, Telecable, and Scripps Howard each have less than 5% totaling 32.8% in all.	Jun-80
USA Network	61.2	Viacom 50%	Apr-80
Nickolodeon/Nick at Nite	60.9	Viacom 100%	Apr-79
Discovery	60.5	TCI 49%, Cox 24%, Newhouse 24%	Jun-85
TBS	60.5	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR, Telecable, and Scripps Howard each have less than 5% totaling 32.8% in all.	Dec-76
TNT	60	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR, Telecable, and Scripps Howard each have less than 5% totaling 32.8% in all.	Oct-88
C-Span I	59.8	1/	Mar-79
MTV	59.5	Viacom 100%	Aug-81
Lifetime	58.6	None	Feb-84
TNN (The Nashville Network)	58.1	Gaylord Broadcasting Co. 100%	Mar-83
Family	57.9	Liberty Media/TCI 18.1%	Apr-77
Arts & Entertainment Network	57.1	None	Feb-84
The Weather Channel	55.4	None	May-82
Headline News	53.2	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR, Telecable, and Scripps Howard each have less than 5% totaling 32.8% in all.	Jan-82
CNBC	50.6	None	Apr-89
VH-1	49.6	Viacom 100%	Jan-85
QVC	46.3	Liberty Media/TCI 28.2%,Comcast 16.4%, Time Warner 10.7%. Cablevision, Colony, Continental, Newhouse, Sammons, and Times Mirror each have less than 5% totaling 42% in all. 2/	Nov-86
AMC (American Movie Classics)	44.5	Cablevision 75%	Oct-84
BET	39.6	TCI 21.4%, Time Warner 17.7%	Jan-80
WGN	35.1	None	Nov-78
Prevue Channel	32.3	None	Jan-88
EWTN	32	None	Aug-81
Comedy Central	30.3	Time Warner 50%, Viacom 50%	Apr-91
C-Span II	29.7	1/	Jun-86

This table was derived from the Economists Inc. study, which was submitted as part of NCTA's Comments, Attachment C, Table 3. Ownership data was derived from Table 6, and sources cited therein, and includes both direct and inderect ownership interests.

1/ According to the NCTA, cable affiliates provide 95 % of funding but have no ownership or program control interests. *SEE* NCTA Comments, Attachment C, Table 3.

2/ Comcast and Liberty Media have reportedly created a partnership to hold QVC interests, through which Comcast would own 57.56%

Table 8

Vertical Integration: Top Fifteen Programming Services (By Primetime Rating)

Rank	Service	Launch	MSOs with Ownership Interest
1	USA Network	Apr-80	Viacom 50%
2	TBS	Dec-76	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR, Telecable and Scripps Howard have less than 5% totaling 32.8% in all.
3	TNT	Oct-88	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR, Telecable and Scripps Howard have less than 5% totaling 32.8% in all.
4	ESPN	Sep-79	None
5	Cartoon	Oct-92	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR, Telecable and Scripps Howard have less than 5% totaling 32.8% in all.
6	Nickolodeon/Nick at Nite	Apr-79	Viacom 100%
7	Lifetime	Feb-84	None
8	Family	Apr-77	Liberty Media/TCI 18.1%
9	Arts &Entertainment	Feb-84	None
10	Discovery	Jun-85	TCI 49%,Cox 24%, Newhouse 24%
11	TNN	Mar-83	Gaylord Broadcasting 100%
12	CNN	Jun-80	Time Warner 19.5%, TCI 23.3%, Times Mirror, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, TKR and Scripps Howard have less than 5% totaling 32.8% in all
13	MTV	Aug-81	Viacom 100%
14	BET	Nov-78	TCI 21.4%, Time Warner 17.7%
15	Sci-Fi	Sep-92	Viacom 50%

Ranking source: *Average Prime-Time Ratings 1994*, Cable TV Programming, August 29, 1994 at 6.

This table was derived from the Economists Inc. study. NCTA Comments, Attachment C, Table 4. Ownership data was derived from Table 6, and sources cited therein, and includes both direct and indirect ownership.

Table 9

National Programming Services with 50% or Greater Ownership Interests by Cable Operators

Ownership Interests	Service (rank)	Total Subscribers of MSOs with Ownership Interests	Potential Market Penetration	Actual Subscribers	Actual Market Penetration
Cablevision 50%, NBC 50%	Bravo	2,155,000	3.63%	12,650,000	21.32%
Gaylord Broadcasting 100%	KTVT	63,195	0.11%	2,400,000	4.05%
	TNN (11)			58,100,000	97.92%
Gaylord Broadcasting 67%, Group W Satellite 33%	Country Music Television			25,900,000	43.65%
Jones Intercable/Jones Spacelink	Mind Ext. Univeristy	1,261,000	2.13%	25,000,000	42.14%
Lenfest 50%(voting control), Liberty Media 7%, Newhouse 17%	The Box	12,538,060	21.13%	16,000,000	26.97%
Cablevision 75%, NBC 25%	American Movie Classics AMC	2,155,000	3.63%	44,500,000	75.00%
Liberty Media 40% (79% voting control)	Home Shopping Network I	10,484,060	17.67%	21,000,000	35.39%
	HSN II			13,000,000	21.91%
Liberty Media 90%, John Sie 10%	Encore			4,100,000	6.91%
Viacom 100%	All News Channel	1,096,000	1.85%	n/a	n/a
	Flix!			125,000	0.21%
	The Movie Channel			2,700,000	4.55%
	MTV (13)			59,500,000	100.28%
	MTV Latino			640,000	1.08%
	Nickolodeon (5)			60,900,000	102.64%
	Nick at Nite (5)			51,250,000	86.38%
	Showtime			7,600,000	12.81%
	VH-1			49,600,000	83.60%
Viacom 50%, MCA 50%	Sci-Fi Channel			15,600,000	26.29%
	USA Network (1)			61,200,000	103.15%
Time Warner 100%	Cinemax	7,232,000	12.19%	6,900,000	11.63%
	HBO			17,900,000	30.17%
Time Warner 50%, Viacom 50%	Comedy Central	8,328,000	14.04%	30,300,000	51.07%

Ownership data derived from Table 6 and includes both direct and indirect ownership interests. Total U.S. basic cable subscriber numbers derived from NCTA Comments, Attachment B. Programming service subscribers derived from *Database*, Cablevision, Apr. 25, 1994, at 44.

Table 10

Programming Services with Minority Ownership Interests by Cable Operators

One MSO With Minority Ownership Interests

Ownership Interests	Service (rank)	Total Subscribers of MSOs with Ownership Interests	Potential Market Penetration	Actual Subscribers	Actual Market Penetration
Liberty Media 18.1%, Public 47.7%, Regent 10.3%, CBN 4.9%, Class A 10.3%, Mgmt 3.7%	Family (10)	10,484,060	17.67%	57,900,000	97.59%
Liberty Media 18%	Cable Health Club			600,000	1.01%
Reiss Media 100%	Request 3-5	10,484,060	17.67%	n/a	n/a
(TCI/News Corp majority owner)	Request Television			17,000,000	28.65%
	Request Television 2			n/a	n/a

Multiple MSO Owners With Aggregate Interests Greater Than 50%.

Ownership Interests	Service (rank)	Total Subscribers of MSOs with Ownership Interests	Potential Market Penetration	Actual Subscribers	Actual Market Penetration
Adelphia Communications, CVI, Colony, Continental, C-TEC, Landmark, Scripps-Howard, Tribune, Times Mirror	Television Food Network	10,682,000	18.00%	7,500,000	12.64%
Continental 12%, Comcast 11%, Cox 20%, Newhouse 11%, Telecable, Viacom 11%,	Viewers Choice 1	19,079,000	32.16%	12,000,000	20.23%
Time Warner 17%, Disney	Viewers Choice 2			4,000,000	6.74%
	Viewers Choice Continuous Hits 1			2,000,000	3.37%
	Viewers Choice Continuous Hits 2,3			n/a.	n/a
Liberty Media 28.2%,Comcast 16.4%, Time Warner 10.7%, Barry Diller 2.3 %, Cablevision, Colony, Continental, Newhouse, Sammons, Times Mirror each hold less that 5%,	QVC	29,976,060	50.52%	46,300,000	78.04%
totalling 42%	QVC Fashion Channel			7,600,000	12.81%
Liberty Media 33%, Time Warner 33%, Cablevision 16.7%, NBC 16.7%	Court TV *	19,871,060	33.49%	14,800,000	24.94%
Liberty Media 38%, Cablevision 25%	Prime SportsChannel Network	12,639,060	21.30%	n/a.	n/a
	NewSport			n/a.	n/a

Table 10

Owners	Service (rank)	Total Subscribers of MSOs with Ownership Interests	Potential Market Penetration	Actual Subscribers	Actual Market Penetration
TCI 10.03%, Cox 10.3%, Continental 10.3%, Comcast 10.3%, Newhouse 10.3%, Time Warner 48.3%	E! (Movietime) *	26,468,060	44.61%	26,000,000	43.82%
TCI 49%,Cox 24%, Newhouse 24%, John Hendricks 3%	Discovery (6)	13,662,060	23.03%	60,500,000	101.97%
	The Learning Channel			28,300,000	47.70%
Ted Turner 28%, Time Warner 19.5%, TCI 23.3%, Cablevision, Comcast, Continental, Jones, Lenfest, Sammons, Times Mirror, TKR, Telecable, Scripps Howard hold less than 5% each for a total of 32.8%	Cartoon Network	31,749,060	53.51%	10,200,000	17.19%
	CNN (9)			61,600,000	103.82%
	Headline News (14)			53,200,000	89.66%
	TBS (2)			60,500,000	101.97%
	TNT (3)			60,000,000	101.13%
	Turner Classic Movies			n.a	n/a

Multiple MSO Ownership With Aggregate Interests of Less Than 50%

Ownership Interests	Service (rank)	MSOs with Ownership Interests	Potential Market Penetration	Actual Subscribers	Actual Market Penetration
Robert Johnson 55.2%, Liberty Media 21.4%, Time Warner 17.8%	Action Pay Per View	17,716,060	29.86%	6,300,000	10.62%
	BET			39,600,000	66.74%

Ownership data derived from Table 6 and includes both direct and indirect ownership interests. Total U.S. basic cable subscriber numbers derived from NCTA Comments, Attachment B. Programming service subscribers derived from *Database*, Cablevision, Apr. 25, 1994, at 44.

* Court TV and E! are managed by divisions of Time Warner. *See* Time Warner, Inc., *1993 Annual Report* at 48.

APPENDIX H

ECONOMIC CONCEPTS FOR ASSESSING THE EXTENT OF COMPETITION IN VIDEO PROGRAMMING DISTRIBUTION MARKETS

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1. This Appendix describes certain economic concepts applied in this *Report* but not fully explained in the text of the *Report* itself. Additionally, certain additional economic information and analysis are provided that supplement the discussion in Section V that addresses the status of competition in multichannel video distribution markets. More specifically, Section I of this Appendix reviews the demand-side concepts of *own-price elasticity of demand*, *market power*, the *implicit Lerner Index*, and the *q ratio*. Section II reviews the supply-side concepts of *economies of scale and scope* and *barriers to entry*. The distinction between *fixed* and *sunk costs* is emphasized together with a brief analysis of the possible effects of sunk costs on long term market structure for local multichannel video programming distribution markets. Finally, Section III briefly addresses certain methodological issues raised in the *Notice of Inquiry* in this proceeding.

I.
DEMAND-SIDE CONCEPTS: MARKET POWER, OWN-PRICE ELASTICITY OF DEMAND, AND THE LERNER INDEX

A. Own-Price Elasticity of Demand and Market Power

2. The nature of demand for any product or service is an important basic condition affecting market structure. In particular, the degree of consumer price sensitivity or to *own-price elasticity of demand*, is an indicator of the availability of competing substitute products or services.[1] If consumer demand at observed market prices tends to be relatively insensitive to the level of market price, then it is likely that the product or service faces extremely limited competition from actual or potential substitute goods. If the supplier of such a product or service is a monopolist, then it is possible that observed market price will exceed the price that would otherwise prevail if either more competitors were supplying the market or other products or services were highly substitutable for the given product or service. In other words, measures of end-user price sensitivity are important in assessing the *market power* of suppliers.

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[1] Own-price elasticity of demand, η, is defined in this Appendix as the absolute value of the percentage change in the quantity demanded (or movement along a given demand curve) for a given percentage change in unit price, all other things, such as product or service quality, held constant. It is understood that the own-price of output varies inversely with the quantity demanded, and the negative sign associated with measures of own-price elasticity is suppressed for simplicity. Demand is *elastic* at the current price and output if $|\eta| > 1$; the percentage change in quantity demanded exceeds the percentage change in price. If $|\eta| < 1$, demand is *inelastic*. If consumers are very sensitive to changes in price, then demand will be elastic as small price increases greatly reduce the quantity purchased of any given good or service. For example, an own-price demand elasticity of $|\eta| = 2$ implies a 20% decrease in quantity demanded will follow a 10% increase in price. Conversely, if consumers are not very sensitive to price changes, demand will tend to be inelastic.

3. Market power refers to the ability of a firm, or group of firms, to set price profitably above the competitive level and maintain such a price over time without attracting competitive entry. In a perfectly competitive market, equilibrium price is equal to marginal cost.[2] Thus, if output price persistently remains above marginal cost over time, the firm does not face perfect competition and has, at least, some market power. The *existence* of market power is distinguished, however, from the *extent* of market power, since small deviations from marginal cost pricing will not, in general, imply serious distortions in market performance.

B. The Implicit Lerner Index

4. To assess the extant market power of local cable systems, this *Report* applies two commonly used measures of market power, namely, (1) the *Lerner Index*; and (2) the *q Ratio*. The Lerner Index establishes a direct relationship between market power and the own-price elasticity of demand and is defined as $L = [(p - MC)/p]$, where p and MC measure the unit output price and the marginal cost of production, respectively. The q ratio is the ratio of the market value of cable system assets to the replacement value of such assets and is described in Section I.C of this Appendix.

5. In most cases, it is difficult to compute reliable estimates of marginal cost at the equilibrium level of output. Consequently, *direct* estimates of the Lerner Index of market power are often impossible to compute. As an alternative methodology, the first-order condition for monopoly profit maximization can be used to compute an *implicit* estimate of the Lerner Index. The divergence of price from marginal cost can be formalized as the *Implicit Lerner Index* of market power which is given by the formula $L = [(p - MC)/p] =$

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[2] A high price-cost margin, i.e., [(p - MC)/p], where p measures the unit price of output and MC measures the marginal cost of production, does not necessarily imply that the firm earns *excess economic profits*, i.e., revenues in excess of what is required to compensate all inputs of production their opportunity costs. If the technology of production implies economies of scale at the observed level of production, then marginal cost for a single output will be *less* than average cost, and setting price equal to marginal cost will result in total revenue less than the total cost of production. Thus, the firm will necessarily set price *greater* than marginal cost, although no excess economic profits will be realized if total cost just equals total revenue. Under these special circumstances, output prices that (1) represent different markups over the marginal cost of production for each output as determined by the own-price elasticity of demand for each individual output, and that (2) constrain the the sum of markups over marginal cost for all outputs to just recover the total shortfall in revenue that might otherwise result if prices were set at marginal cost are called *Ramsey prices* and represent second-best, economically-efficient prices in the presence of economies of scale. In the case of a single output, the Ramsey price is equal to the average cost of production for any given level of output. For further discussion of Ramsey pricing, see William J. Baumol & David F. Bradford, *Optimal Departures from Marginal Cost Pricing*, 60 AM. ECON. REV. 265-83 (1970). *See* also STEPHEN J. BROWN & DAVID S. SIBLEY, THE THEORY OF PUBLIC UTILITY PRICING ch. 3 (1986).

$(1/|\eta|)$, where η measures the own-price elasticity of demand.[3] Given reliable estimates of the own-price elasticity of demand, η, the extent of market power can be *inferred* indirectly without the requirement of estimating marginal cost at the profit-maximizing level of production.

6. The Lerner Index is a measure of the extent of market power. If the elasticity of demand for a firm's product is infinite, as it is in a perfectly competitive market, then the deviation of price from marginal cost is zero. As illustrated by the Lerner Index, the larger in absolute value is the own-price elasticity of demand, the smaller the divergence between monopoly and competitive price, where competitive price is just equal to marginal cost in the absence of economies of scale.[4] As the number of substitutes for cable service increases, the elasticity of demand for video programming services offered by incumbent cable systems will increase. Thus, even if competition in local cable markets is between a few firms selling somewhat differentiated products, such rivalry may significantly increase the elasticity of demand for each of the rivals' services and eliminate significant deviations of price from marginal cost.

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[3] The Implicit Lerner Index is itself subject to important limitations. For example, it is assumed that the estimate of the own-price elasticity of demand used to estimate the Implicit Lerner Index corresponds to the profit-maximizing value of the own-price elasticity of demand along the monopolist's demand curve. This assumption may or may not be troublesome, depending on the correct specification of the firm's demand function. If the correctly-specified demand function facing a cable system is linear, then the own-price elasticity of demand will vary continuously as the quantity demanded changes. Conversely, if the correctly-specified demand function is log-linear, then the own-price elasticity of demand is constrained to a constant value regardless of the level of quantity demanded. If quantity demanded is specified as the penetration rate, a logit transformation of the penetration rate allows for estimation of the own-price demand elasticity at different levels of quantity demanded, i.e., penetration rates. *See* KENT WEBB, THE ECONOMICS OF CABLE TELEVISION ch. 4 (1983). To avoid possible bias in the measurement of the extent of market power induced by selecting an incorrect estimate of the own-price elasticity of demand, a range of possible own-price elasticities of demand found in the empirical literature was assumed to "bracket" correct values. In addition, empirical own-price elasticities inconsistent with monopoly profit-maximization were excluded. See Section I.D and Table H-1 in this Appendix.

[4] When measuring the extent of market power of a given firm, the *market* and the *firm* demand curves must be carefully distinguished. If the entire market is served by a single firm, i.e., a monopoly, then the market demand curve is equivalent to the firm demand curve. Under perfect competition, each firm's demand curve is perfectly elastic and the market demand curve does not coincide with the firm demand curve. To the extent that monopoly cable systems begin to face competition from overbuilders or other technologies for distributing multichannel video programming, then local cable operators will face a *residual demand curve* -- the horizontal distance between the market demand curve and the total fringe supply -- that will tend to become more elastic over time and, therefore, tend to decrease the incumbent's market power.

7. If the own-price demand elasticity of a dominant firm facing some competition is not known, the *market share* of the dominant firm, i.e., the percentage of total industry output supplied by the firm, can sometimes be used to compute the extent of market power. Given certain assumptions, the market power of a dominant firm, such as a local cable system beginning to face some competition, can be estimated using an estimate of the firm's market share; the own-price elasticity of the market demand curve; and the *supply elasticity* of rival firms, i.e., the percentage increase in quantity supplied by rival firms given a one percent change in output price. In this case, the Lerner Index, or the price-cost margin, can be written more generally as $L = S_D/[\eta_m+\varepsilon_s(1 - S_D)]$, where S_D is the market share of the dominant firm; η_m is the market own-price demand elasticity; and ε_s is the supply elasticity of the rival or fringe firms.[5] From this equation, it is apparent that the larger the market share of the dominant firm, the greater its market power, other things remaining the same. The larger (in absolute value) the market demand elasticity, other things equal, the larger will be the dominant firm's own-price demand elasticity and the smaller the deviation of price from marginal cost. The larger the supply elasticity of the competitors, measured by the ability of existing firms to increase output as well as new firms to enter the market, the larger the own-price demand elasticity of the dominant firm and, therefore, the lower its market power.[6]

C. The q Ratio

8. An alternative measure of market power is the q ratio, which is the ratio of the market value of a firm (measured by the market value of its outstanding stock and debt) to the replacement cost of the firm's physical assets.[7] If the market value of a firm is greater than its replacement cost, excess economic profits are being earned.[8] The market value of a

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[5] See William M. Landes & Richard A. Posner, *Market Power in Antitrust Cases*, 94 HARV. L. REV. 937-96 (1981).

[6] The simple, inverse-elasticity Lerner Index is a special case of the market-share Lerner Index just described. If the entire output of a single-product industry is supplied by a single firm, the market share of that firm is 100%, and the market demand curve is equivalent to the firm demand curve. In this special case, the market-share Lerner Index collapses into the simple, inverse-elasticity Lerner Index. Under these circumstances, η_m is equal to η, and the expression $\varepsilon_s(1 - S_D)$ reduces to zero, since S_D is equal to one. An assumption inherent in the simple, inverse-elasticity Lerner Index is that the monopoly firm faces no potential competitors or that such potential competitors do not as yet provide any constraint on the exercise of monopoly power by the monopoly firm.

[7] The q ratio as an indicator of market performance was proposed by James Tobin. See James Tobin, *A General Equilibrium Approach to Monetary Theory*, 1 J. MONEY CREDIT & BANKING 15-29 (1969).

[8] DENNIS W. CARLTON & JEFFREY M. PERLOFF, MODERN INDUSTRIAL ORGANIZATION 343 (2d ed. 1994).

firm consists of three components, namely, the capitalized value of rents attributable to monopoly power; scarce factors of production; and the firm's existing capital stock.[9] The magnitude of the capitalized value of these rents is reflected by the extent that the q ratio exceeds one.[10] The size of these rents reflects earnings in excess of the amount necessary to compensate all factors of production at rates equal to their full opportunity cost. The q ratio is a measure of long-run profitability, which makes it useful for measuring monopoly power for public policy considerations.[11] The q ratio is often a preferable measure of profitability compared to the price-cost margin, since the difficulties in measuring marginal cost are avoided.

9. While the q ratio is an alternative to the Lerner Index as a measure of market power, the two measures can be directly linked under certain conditions. It can be shown that $q = 1+(1/|\eta|)(R/K)[1/(\rho - g)]$, where R is the firm's revenue for a given period of time; K is the dollar value of the firm's capital stock; $(1/|\eta|)$ is the simple Lerner Index; ρ is the long term discount rate; and g is the projected long term percentage growth rate of revenue.[12] From this equation, it is apparent that the Lerner Index $(1/|\eta|)$ and the q ratio tend to be correlated: large q ratios will be associated with large Lerner Indices, other things remaining constant. Much like the simple, inverse-elasticity Lerner Index, the q ratio measure of profitability is highly sensitive to the own-price elasticity of demand. If the firm sells its output in perfectly competitive output markets, then the firm's own-price elasticity of demand approaches infinity, and its inverse, $(1/|\eta|)$ or the simple Lerner Index, necessarily approaches zero in value. As a result, the expression $(1/|\eta|)(R/K)[1/(\rho - g)]$ must also approach zero, and the q ratio converges to one in value, where by definition, the firm possesses no market power. Thus, it is apparent that q values in excess of one imply the exercise of market power, absent measurement problems or substantial violations of other assumptions inherent in the definition of q.

10. As noted in the *1990 Report*, q ratios in excess of one may be attributable to factors other than excess economic profits. Since the q ratio is a fraction, incorrect estimates in either the numerator or denominator can have significant effects on the q estimates. Thus, inaccurate measures of either the market value or replacement costs of a firm's tangible assets

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[9] Michael Spirlock, Thomas Gilligan, & William Marshall, *Tobin's q and the Structure-Performance Relationship*, 74 AM. ECON. REV. 1051-60 (1984).

[10] *Id.*

[11] Michael A. Salinger, *Tobin's q, Unionization, and the Concentration-Profits Relationship*, 15 RAND J. ECON. 159-70 (1984).

[12] *Id.* at 161. This definition of the q ratio assumes long-run equilibrium with constant returns to scale in the production of output; no taxes or inflation; and all future profits accrue to capital. If the production process is characterized by economies of scale, then the simple Lerner Index, $[(p - MC)/p] = 1/|\eta|$, must be replaced with $[(p - AC)/p]$ where p is the unit price of output and AC is the average cost of production. Therefore, the q ratio, under increasing returns to scale, reflects the markup of price over the average cost of production.

can produce imprecise and misleading measures of q.

11. In general, the market value of a firm, the numerator of the q ratio, can be accurately estimated by summing the value of securities, i.e., stocks and bonds, issued by the firm. This approach is referred to as the "public" market value. However, if stock market values are extremely volatile, then this approach will produce less reliable estimates of firm value.[13] For example, if the data are limited to a specific year, or even month, the value of securities may produce misleading estimates of the q ratio, if stock prices are abnormally high at that given time. This particular problem is minimal if stock prices are not volatile or the data are drawn from different time periods.

12. It is far more difficult, however, to obtain an estimate of the replacement value of the firm, the denominator of the q ratio. One particular measurement problem is the exclusion of the value of intangible assets, such as goodwill, in the estimate of replacement cost. If advertising, or some other factor, generates a positive amount of goodwill, the q ratio will typically exceed one, since goodwill will increase the market value of the firm but not its replacement value. In addition, since the assets of the firm are "used," estimated replacement costs may be affected by the particular accounting method chosen to adjust the assets for depreciation.[14] Again, inaccuracies in the measurement of replacement cost will result in a q ratio greater than one, even if excess economic profits are zero.

13. Moreover, a particular firm's q ratio may be greater than one as a result of superior management skills or exceptionally efficient productive methods. Neither of these factors will be reflected in the estimate of replacement cost, but both will most likely affect the market value of the firm. It seems unlikely, however, that superior management skills or efficient production techniques can explain a significant portion of a cable firm's profits, given the current lack of effective competitive constraints on cable operators. Therefore, these factors are unlikely to have a significant effect on estimates of q for many, if not most, cable systems today.[15]

14. Notwithstanding the possible conceptual limitations of the q ratio as a measure of market power, the estimated q ratios reported in Table 5.2 in the text of this report are so

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[13] *See* R.J. Shiller, *Do Stock Prices Move Too Much to Be Justified by Subsequent Changes in Dividends?*, 71 AM. ECON. REV. 431-36 (1981).

[14] For a comprehensive analysis of these issues, *see* Spirlock, Gilligan, & Marshall, *supra* note 9.

[15] While high profits may be related to risk rather than monopoly power, the q ratio includes an automatic adjustment for risk. *See* Salinger, *supra* note 11; Spirlock, Gilligan & Marshall, *supra* note 9. With respect to superior management skills, the value of the firm will only be affected to the extent that the managers do not capture for themselves the rents produced by their skill. The effects of superior management skills on the value of cable systems are addressed in the *1990 Cable Report*, Appendix E.

far above the benchmark value of one that it appears difficult to contradict the hypothesis of substantial market power in local cable distribution markets. Details describing the estimation of the q ratios and the pertinent assumptions made in the various computations are provided in Appendix I.

D. Empirical Studies on the Own-Price Elasticity of Demand for Basic Cable Services

15. The calculation of implicit Lerner Indices requires robust econometric estimates of the own-price elasticity of demand for cable services, especially basic cable service. Fortunately, a number of recent econometric studies of the demand for basic cable service report estimates of the own-price elasticity of demand. These econometric studies provide various estimates of the own-price elasticity of demand for both basic and pay cable services. The econometric estimates of own-price elasticities for some of the more recent empirical studies are reported in Table H-1.[16] Most empirical studies relate the unit price of cable service to either (1) the *number of subscribers* or (2) the *penetration rate* defined as the number of households subscribing to either basic or pay cable service divided by the number of households passed by cable.[17] The own-price elasticity estimates are broadly similar

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[16] *See* * Robert W. Crandall, *Elasticity of Demand for Cable Services and the Effect of Broadcast Signals on Cable Prices*, paper appended to *TCI Reply Comments* in Mass Media Docket 90-4; ** Robert N. Rubinovitz, *Market Power and Price Increases for Basic Cable Service Since Deregulation*, 24 RAND J. ECON. 1-18 (Spring 1993); *** Tasneem Chipty, *Horizontal Integration for Bargaining Power: Evidence from the Cable Television Industry*, paper presented at the *AEI Telecommunications Summit: Competition and Strategic Alliances*, American Enterprise Institute, July 7, 1994; **** J. Mayo and Y. Otsuka, *Demand, Pricing and Regulation; Evidence From the Cable TV Industry*, 22 RAND J. ECON. 396-410 (Autumn 1991); ***** R. Beil, T. Dazzio, R. Ekelund & J. Jackson, *Competition and the Pricing of Cable Television Services*, 6 J. REG. ECON. 401-15 (December 1993); ****** George Ford, Competition in the Cable Television Industry: An Economic Analysis of Overlap Variations and Cable Prices (unpublished doctoral dissertation completed at Auburn University, 1994).

[17] The penetration rate expresses the number of subscribers in relation to the *potential* market demand for any defined franchise area, *i.e.*, homes passed. The penetration rate provides several advantages as a measure of cable system demand. First, since the penetration rate is measured as a ratio or percentage, it is not affected by the size of the cable system. Thus, penetration rates for both large and small cable systems can be usefully compared. Second, weighting the quantity of subscribers by the reciprocal of homes passed corrects for heteroskedasticity in the regression analysis. Using the penetration rate as a quantity measure neither affects the interpretation of demand elasticity nor its relevance in calculating the Lerner Index, as the penetration rate is merely an alternative measure of quantity demanded. Since demand elasticity is itself dimensionless, it should be unaffected by the penetration rate transformation.

despite different econometric specifications, estimation methodologies, and data sets.[18]

16. The Crandall study estimates two demand model specifications, namely, Specification 1 that constrains the estimated elasticity to be a constant for all values of cable price and number of subscribers; and Specification 2 that permits the estimated elasticity to vary for different values of cable price and number of subscribers. As shown in Table H-1, the estimated own-price elasticities were not dramatically affected by the different instrument sets. Crandall's results suggest that the own-price elasticity of demand for basic cable service tends to be elastic, ranging from approximately 1.6 to 3.4, depending upon the model specification and instrument set. The Rubinovitz and Beil, et al., studies also show that the demand for basic cable tends to be elastic, although somewhat less elastic than shown in the Crandall study. Mayo and Otsuka find demand to be close to unity across the markets in their sample. According to their estimates, demand elasticities tend to be higher in urban areas and larger television markets. The Chipty study estimates own-price elasticities of demand for both basic and pay cable service. Again, these empirical estimates tend to show that the demand for basic (and pay) cable services are elastic. Finally, the Ford study shows that in duopolistically-competitive cable markets, the demand curve faced by the cable system operator is more elastic than in markets where competition is absent, i.e., in monopoly markets.

17. Notwithstanding the differing econometric methodologies and data sets, the demand elasticities reported in Table H-1 generally suggest that the demand for cable television tends to be elastic. To the extent that existing cable rates exceed the incremental cost of production, rate reductions should be expected to increase the number of subscribers and levels of penetration, and increase revenues for local cable systems, while possibly reducing local cable system profits. To the extent that local cable rates are the result of

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[18] None of the studies on overbuild competition provide an estimate of the *cross-price elasticity of demand*, i.e., the extent to which the quantity sold of one firm's product is affected by a change in the price of a related product, other things remaining the same. If the cross-price elasticity is positive, the products are *substitutes*; if negative, the goods are *complements*. Given that the own-price demand elasticity for a product or service is affected by the number of substitutes for that product or service, it can be shown that the higher the positive value of the cross-price elasticity between two rival cable operators' services, the larger will be the absolute value of a firm's own-price elasticity of demand for its particular services. Thus, the larger the cross-price demand elasticities between the services offered by two rival cable firms, the less likely it is that either firm will possess significant market power, since market power is inversely related to the own-price demand elasticity as illustrated by the implicit Lerner Index. For a general discussion of cross-price elasticity, including its relationship to the own-price elasticity of demand, see CARLTON & PERLOFF, *supra* note 8, at 807. Today, econometric estimation of cross-price demand elasticities between rival cable operators is hindered by multiple problems, including the wide variations in the extent of system overlap between competing systems and other data and statistical difficulties. As competition develops in the cable industry, estimating cross-price elasticities may become feasible.

monopoly power exercised by local cable systems, additional competition should result in rate reductions for basic cable service as the elasticity of demand for the cable operator increases, a result consistent with the results reported in Ford's study.

TABLE H-1

ECONOMETRIC ESTIMATES OF OWN-PRICE ELASTICITY OF DEMAND FOR CABLE TELEVISION

Study	Demand Measure		Own-Price Elasticity Estimate ($\|\eta\|$)
	Number of Subscribers	Penetration Rate	
Crandall (1990)*			
Instrument Set A			
Specification 1	X		1.760
Specification 2	X		2.329
Instrument Set B			
Specification 1	X		2.134
Specification 2	X		3.375
Instrument Set C			
Specification 1	X		1.578
Specification 2	X		2.151
Rubinovitz (1993)**	X		1.46
Chipty (1994)***			
Basic Cable			
Minimum Value		X	1.054
Maximum Value		X	2.387
Mean Value		X	1.877
Pay Cable			
Minimum Value		X	1.050
Maximum Value		X	3.748
Mean Value		X	2.029
Mayo and Otsuka (1991)****			
Top 50 Markets			
Urban		X	1.51
Suburban		X	1.05
Second 50 Markets			
Urban		X	1.22
Suburban		X	0.98
Below Top 100 Markets		X	0.81
Average		X	0.969
Beil, et al (1993)*****		X	1.09
Ford (1994)******			
Specification A			
Monopoly		X	0.87
Duopoly		X	1.51
Specification B			
Monopoly		X	1.31
Duopoly		X	2.62

Source: References cited in footnote 16.

E. Empirical Estimates of the Implicit Lerner Index

18. The econometric estimates of the own-price elasticity of demand reported in Table H-1 that are consistent with the theoretical conditions for profit-maximization range from 1.054 to 3.375.[19] Table H-2 reports estimates of the Implied Lerner Indices using a representative sample of the own-price elasticities reported in Table H-1. Table H-2 also reports the *Implied Markup Factors* that are derived from an algebraic restatement of the Lerner Index. The Implied Markup Factor expresses the profit-maximizing price as some multiple of marginal cost. Firms selling their output in a perfectly competitive market would set price equal to marginal cost, implying a markup factor equal to one. Markup factors in excess of one are indicative of market power. Similarly, the value of the Lerner Index for a firm selling in perfectly competitive output markets is zero, since a competitive firm does not realize any markup over the marginal cost of production.

TABLE H-2

IMPLICIT LERNER INDICES
FOR CABLE SYSTEMS

Econometric Study	Basic Service Own-Price Elasticity of Demand $[\lvert\eta\rvert]$	Implied Lerner Index $[1/\lvert\eta\rvert]$	Implied Markup Factor $[\lvert\eta\rvert/(\lvert\eta\rvert - 1)]$
Rubinovitz (1993)	1.46	0.69	3.17
Chipty (1994)	1.88	0.53	2.14
Crandall (1990)			
Specification B1	2.13	0.47	1.88
Specification B2	3.38	0.30	1.42
Ford (1994)			
Monopoly	1.31	0.76	4.22
Duopoly	2.62	0.38	1.61

Source: Table H-1.

[19] An unconstrained profit-maximizing firm will always price its output in the elastic region of its demand curve where the absolute value of the own-price elasticity of demand is greater than 1. *See* CARLTON & PERLOFF, *supra* note 8, chs. 1, 9.

19. If it is assumed that local cable systems attempt to set profit-maximizing prices for basic cable service, then the presence of market power is implied for the range of empirical estimates of the own-price elasticity of demand shown in the second column of Table H-2.[20] The Implied Lerner Index suggests that the percentage markup over profit-maximizing price, i.e., [(p - MC)/p], ranges from thirty to seventy-six percent. Similarly, the Implied Markup Factors range from 1.42 to 3.50.[21] With regard to overbuild competition, the Implied Markup Factors produced using Ford's own-price demand elasticity estimates clearly show that such competition diminishes market power.

II.
SUPPLY-SIDE CONCEPTS

A. Economies of Scale and Scope

20. Changes in the cost of production as output expands may have an important effect on market structure. If, for example, the average cost of production is little affected by the quantity produced by any given firm in an industry, then the market might be supplied by many firms, with no individual firm having any important cost advantage relative to any other. In other words, the *scale* of production does not affect the cost of production for any firm in the industry. Under these circumstances, market structure may resemble a perfectly competitive industry, unless various types of barriers to entry preclude competitive entry.

21. Conversely, should the expansion of output by any given firm result in a *reduction* in the average cost of production as higher-capacity facilities are used to produce higher volumes of output, then market structure may be dominated by a few firms that supply the entire market. In such a case, each firm realizes *economies of scale* in the production of output, although such production economies are usually exhausted at sufficiently large

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[20] Crandall, in his study cited in Table H-2 that uses TCI cable system cost data, estimates the price-cost ratio for a representative TCI cable system as approximately 2.0. This price-cost ratio is quite close to the implied markup factor of 1.88 implied by Crandall's estimated own-price elasticity of demand equal to 2.134 as shown in Table H-2. To the extent that TCI cable systems are broadly representative of cable systems more generally, estimated own-price elasticities for basic cable service in the vicinity of 2.0 are probably consistent with profit-maximizing prices for basic cable service. See Robert W. Crandall, *supra* note 16, at 2-8.

[21] The Implied Lerner Indices and Implied Markup Factors shown in Table H-2 are only *suggestive* of market power in local multichannel video programming distribution markets dominated by local cable systems. If the production of local cable services is subject to some economies of scale and scope in the longer term, then prices may be expected to exceed marginal cost. In other words, some excess over marginal cost may be required to recover the total cost of production even in the absence of excess economic profit. Consequently, values of Implied Lerner Indices should be compared with other measures of market power, such as q ratios, in order to evaluate the reasonableness of the estimated values.

volumes of production. In a special, limiting case, a *single* enterprise may be able to supply total market demand at least total cost compared to multiple competing suppliers, reflecting the application of a technology of production so technically efficient at large levels of output that only a single supplier is required. Such a firm is called a *natural monopoly*. Often, firms defined as natural monopolies are treated as public utilities and subjected to regulation. Historically, such regulation precludes competitive entry, since, by definition of a natural monopoly, any competitor to the public utility can only produce output at higher average cost and, hence, a higher price to the consumer relative to the prices charged by a regulated natural monopoly firm.[22]

22. The cost structures of firms that supply multichannel video programming to subscribers are likely to be both complex and dynamic over the longer term as new technologies of video programming distribution become more widely available. Analytically, a *multioutput cost function* is a useful tool for understanding the behavior of plant-level costs of production. In particular, such a cost function permits the definition and measurement of *product-specific economies of scale* and *economies of scope*, the cost savings attributable to producing multiple outputs in the same plant using certain shared inputs of production. For a firm that produces a single output, large economies of scale in production may be sufficient to result in a natural monopoly. Most firms, however, produce multiple outputs. The notion of natural monopoly in the case of multiple outputs is necessarily more complicated than the single-output case, although recent theoretical work on the economics of multioutput production have established the cost conditions defining natural monopoly under these circumstances.[23]

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[22] The standard view of single-output natural monopoly implicitly assumes that the natural monopoly firm minimizes the total cost of production for any level of output, notwithstanding the lack of competition that would ordinarily force a competitive firm to behave this way. But without competition to force the natural monopoly firm to minimize the total cost of production, it is both possible and likely that the natural monopoly firm will tolerate *X-inefficiency*, i.e., higher unit cost for any level of output compared to the unit cost of production for a firm that faced competition and consequently minimized its expenditures on the inputs of production. Such X-inefficiency may be expected to persist even if the natural monopoly firm is subject to public utility regulation. Although the idea of X-inefficiency can be traced to Adam Smith, Harvey Leibenstein has advocated its importance in recent years. See Harvey Leibenstein, *Allocative Efficiency vs. X-Efficiency*, 56 AM. ECON. REV. 392-415 (June 1966). A recent collection of articles assessing the state of X-efficiency theory is STUDIES IN ECONOMIC RATIONALITY: X-EFFICIENCY EXAMINED AND EXTOLLED (Klaus Weiermair & Mark Perlman eds. 1990).

[23] The modern theory of multioutput cost functions is fully developed in WILLIAM J. BAUMOL, JOHN C. PANZAR, & ROBERT D. WILLIG, CONTESTABLE MARKETS AND THE THEORY OF INDUSTRY STRUCTURE (1982).

23. Technological change, learning curve effects, and *systems rivalry*[24] between and among competing multichannel video programming distributors may accentuate economies of scale and scope in video programming delivery through time. Such economies do not, however, imply a *natural monopoly market structure* in local video programming distribution markets over the longer term, although such economies may constrain the number of profitable video programming delivery systems in some local markets.[25] Such industry cost conditions are unlikely to represent *policy-relevant barriers to entry*, however, since their realization is likely to be the *result* of systems rivalry rather than an *impediment* to such competition.[26] Some insight concerning the extent of possible economies of scale and scope

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[24] The distribution of multichannel video programming is an example of a *system*, *i.e.*, "collections of two or more components together with an interface that allows the components to work together." Output provided to consumers on networks often implies certain *feedback effects* that may directly affect market structure. A common approach for evaluating feedback effects in network-based markets is studying *market competition between systems* as opposed to competition between products. *See* Michael Katz & Carl Shapiro, *Systems Competition and Network Effects*, 8 J. ECON. PERSP. 93 (1994).

[25] A distinction is drawn between the plant-level technology of production that displays *natural monopoly cost characteristics*, i.e., product-specific economies of scale, economies of scope, or both, and a *natural monopoly market structure*. Many firms, especially firms that tend to be capital-intensive, utilize technologies of production that result in *some* economies of scale or scope in production at observed levels of demand, i.e., reflect natural monopoly cost characteristics. The *extent* of such economies is often insufficient, however, to preclude the entry of rivals that also produce output subject to similar economies of scale and scope. Ordinarily, each entrant differentiates its output from that of its competitors, which, if successful, enhances the consumer's willingness-to-pay for the specific output of the given firm. Thus, even if the incumbent firm could produce total market demand at least total cost, consumers in general do not find the product variety offered by a single firm equivalent to, or even preferred to, the collection of differentiated products and services offered by competing firms. Thus, in most markets, both product-specific economies of scale and economies of scope are never fully realized, since consumers value the benefits of product diversity provided by diverse firms more highly than more homogeneous output produced at lower unit cost and price. By contrast, a natural monopoly market structure will emerge in instances where (1) the technology of production implies product-specific economies of scale, economies of scope, or both that are pervasive and profound; (2) the fixed costs of production are large and almost entirely sunk; and (3) consumers place little or no value on product differentiation. Given these conditions, a monopoly market structure will emerge "naturally" over the longer term, even without government-imposed barriers to entry. Few real-world markets, where entry is free and not constrained by public policy, tend to converge, however, toward natural monopoly as an equilibrium market structure over the longer term.

[26] Policy-relevant entry barriers are discussed in the next section.

is provided by econometric studies of cable system cost functions. Several of these studies are reviewed in the next section.

B. Empirical Studies on Economies of Scale in Cable Television Distribution

24. Rigorous study of the cost structure of local cable systems requires the formulation and estimation of multioutput econometric cost functions. Two empirical studies estimate the cost structure of local cable systems, namely, studies by (1) Owen and Greenhalgh and (2) Noam.[27] Both studies find some evidence of economies of scale, although such economies are not large.[28]

25. Owen and Greenhalgh estimate a fourteen percent cost penalty to overbuilding using data from franchise applications, where output is defined as the number of subscribers.[29] This estimate *overstates* the cost penalty of overbuilding, since total market output is assumed to be constant, i.e., no price competition results from overbuilding. Empirical studies on competition in the cable industry suggest, however, that total market output tends to increase as marginal customers subscribe to basic cable service in response to a reduction in price.[30] When changes in the output of the cable system are measured not only as an increase or decrease in the number of subscribers, but include proportional changes in the amount of institutional (local public, educational, and government) network investment and miles of wire (cable plant), Owen and Greenhalgh's estimates show that the average cost of production is approximately constant with respect to a proportional change in all three measures of output. As noted by the authors and subsequent studies, Owen and Greenhalgh's estimates are troublesome, however, since the franchise application data used in their study are only *estimated* construction and operation expenditures. Such data include the estimates of both efficient and inefficient bidders; could be biased by opportunistic behavior or "gamesmanship;" and ". . . do not clearly reflect the minimum cost based on using best-

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[27] Bruce M. Owen & Peter R. Greenhalgh, *Competitive Policy Considerations in Cable Television Franchising*, 4 CONTEMP. POL'Y ISSUES 69-79 (1986); ELI NOAM, VIDEO MEDIA COMPETITION: REGULATION, ECONOMICS AND TECHNOLOGY (1985).

[28] Given limited data availability, there are few published or publicly-available econometric studies of cost functions for cable firms. Only such econometric studies, however, provide rigorous measures of product-specific economies of scale and economies of scope attributable to multioutput production by a single firm.

[29] In other words, entry of a second cable system forces the incumbent to restrict output (at least initially) and operate at a higher point on its average cost curve, all other things remaining the same. Owen and Greenhalgh estimate the size of this effect as approximately 14% over what cost would have been absent the overbuild competitor.

[30] *See* Beil, Dazzio, Ekelund & Jackson, *supra* note 16.

practice techniques of running a cable system of a given size."[31]

26. In a more sophisticated attempt at measuring scale and scope economies in cable distribution, Noam estimates a series of cost functions using 1981 data for more than 4800 cable systems. His estimates suggest the presence of economies of scale in the production of cable services, but the economies vary according to the definition of output.[32] Product-specific scale elasticity estimates for the outputs defined as "basic subscribers," "pay subscribers," and "homes-passed" are 1.054, 1.074, 1.020, respectively.[33] Product-specific economies of scale are observed for the basic and pay subscriber output measures. The product-specific scale elasticity estimate for the homes-passed measure of output is not statistically different from one, however. These results suggest that economies of scale are observed only in the number of basic and pay subscriptions, and not the physical size of the network, i.e., homes-passed. Taking into account economies-of-scope between the size of the distribution network and the number of subscribers for both basic and pay cable services, Noam's estimates indicate slight economies of scope; the *total scale elasticity* estimate is calculated to be 1.096, implying that a ten-percent decrease (increase) in all outputs in fixed proportion will result in approximately a one-percent increase (decrease) in the cost of production. The scale elasticity estimates from the Noam study (the most sophisticated to date) do not suggest, however, that significant economies of scale -- regardless of the measure of output -- pervade the cable distribution industry.

27. Based on the two econometric cost studies, competitive entry in local multichannel video programming markets may appear to imply some loss in economic benefit

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[31] Owen & Greenhalgh, *supra* note 27, p. 72. A number of studies assert that opportunistic behavior at the franchise stage is significant. *See* Oliver Williamson, *Franchise Bidding for Natural Monopolies -- In General and With Respect to CATV,"* 7 BELL J. ECON. 73-104 (Winter 1976); Robin Prager, *Firm Behavior in Franchise Markets*, 21 RAND J. ECON. 211-225 (Summer 1990).

[32] Data used by Noam consisted of monopoly systems only. The nature of cost under duopolistic competition may be significantly different than under monopoly supply. For example, numerous analysts have suggested the possibility of X-inefficiencies in monopoly markets. *See* NOAM, *supra* note 27; Thomas W. Hazlett, Duopolistic Competition in Cable Television: Implications for Public Policy, 7 YALE J. REG. 65-120 (Winter 1990), at 80; Nelson & Primeaux, *The Effects of Competition on Transmission and Distribution Cost in the Electric Utility Industry*, 64 LAND ECON. 338-46 (1988).

[33] *Product-specific scale elasticity*, ε_s, is defined as the percentage change in output divided by the percentage change in cost, or $\varepsilon_s = [(\%\Delta\text{Output})/(\%\Delta\text{Cost})]$, where values greater than one imply average cost is decreasing as the level of output increases, i.e., economies of scale are present. *Total scale elasticity* measures the change in output as the proportional response of multiple outputs to a proportional increase in the scale of production. Again, values greater than one imply average cost is decreasing as the scale of plant is increased. See W. BAUMOL, J. PANZAR, AND R. WILLIG, *supra* note 23, pp. 73-74.

to consumers, since such entry may prevent the incumbent cable system from fully realizing all the economies of scale and scope inherent in the production of cable services. Such an inference, however, ignores the possible benefits of competitive entry. For example, if *post-entry prices are lower than pre-entry prices*, then cost penalties must be weighed against increases in consumer welfare resulting from lower prices. Therefore, even if economies of scale are present, gains in consumer welfare from *lower* prices may be expected to more than offset the cost penalty of duplicated facilities. As a result, allowing open-entry into local cable markets, where such entry results in lower prices, can increase net social welfare (exclusive of product variety), despite some loss in static economic efficiency resulting from foregone economies of scale.

28. Although local cable distribution networks are probably characterized by slight economies of scale, empirical evidence concerning the favorable price effects of overbuild competition suggest that entry restrictions in local cable markets are likely to be economically-inefficient and detrimental to the welfare of consumers. Given the prospective entry of competitors using different local distribution technologies, such as MMDS, DBS, and LECs, natural monopoly cost characteristics may tend to constrain the number of overbuilders in most local cable markets but need not necessarily constrain the extent of competitive rivalry that should tend to improve consumer welfare over the longer term.

C. Conditions of Entry

29. Barriers to entry and exit are probably the single most important factor influencing market structure. For public policy purposes, however, the concept of barriers to entry should be carefully defined. Bain specified three sources of barriers to entry, namely, (1) the absolute cost advantages of incumbent firms; (2) economies of scale; and (3) the product differentiation advantages of incumbent firms.[34] Stigler proposed a more general definition of barriers to enter, namely, ". . . a cost of producing (at some or every rate of output) which must be borne by a firm which seeks to enter an industry but is not borne by firms already in the industry."[35] Stigler's general definition of a barrier to entry is broadly accepted in many contemporary industrial organization studies. Christian von Weizsäcker proposes a more restricted definition of a barrier to entry that qualifies Stigler's definition, namely, a barrier to entry is ". . . a cost of producing which must be borne by a firm which seeks to enter an industry but is not borne by firms already in the industry and which implies a distortion in the allocation of resources from the social point of view."[36] Weizsäcker's definition of a barrier to entry suggests in effect that the proposed removal of a barrier to entry requires a cost-benefit analysis that identifies all gains in economic efficiency, including relevant externalities, that are derived from the presence of the entry barrier as well as the

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[34] J.W. BAIN, BARRIERS TO NEW COMPETITION (1956).

[35] GEORGE J. STIGLER, THE ORGANIZATION OF INDUSTRY 67 (1968).

[36] C.C. von Weizsäcker, *A Welfare Analysis of Barriers to Entry*, 11 BELL J. ECON 400 (Autumn 1980).

actual or potential losses in economic efficiency resulting from the entry barrier, including all costs implied in eliminating or minimizing its effects.

30. Since some models of market competition establish a direct relationship between the number of firms supplying the market and the quality of market performance, it appears self-evident that any obstacle impeding the free and easy flow of new firms into the market must have a direct and unequivocal adverse effect on market performance.[37] As a result, the elimination of *any* impediment to entry should produce an unambiguous, although possibly small, incremental improvement in market performance and consumer welfare. Following this logic, the "optimal" public policy toward impediments to market entry is, therefore, one of "zero tolerance."

31. Closer examination of a zero tolerance policy toward barriers to entry suggests, however, that such a policy *without important qualifications* is unlikely to be optimal. From a public policy perspective, *not* all impediments, however, are necessarily *barriers to entry* that require some type of government intervention or remediation. For purposes of this *Report*, costs borne by entrants but not incumbents that have adverse affects on consumer welfare are defined as *policy-relevant barriers to entry*.[38] Barriers to entry defined in this way are candidates for regulatory or antitrust scrutiny, where such scrutiny may result in policy recommendations for reducing or eliminating such entry barriers. Such scrutiny should be approached as a cost-benefit analysis that identifies all possible economic efficiencies, if any, that might result from the presence of the barrier to entry; identifies all offsetting economic inefficiencies that might be attributable to the barrier to entry, if any; identifies all relevant positive and negative externalities; and, finally, estimates the economic cost of eliminating the barrier to entry or minimizing its effects.

1. Fixed and Sunk Costs as Barriers to Entry

32. The existence of both scale and scope economies in local cable system networks may represent a limited impediment to unconstrained market entry by potential overbuilders. The essential question is whether such an impediment to entry is also a policy-relevant barrier to entry. Answering this question, however, requires a careful distinction between several types of cost, especially, *fixed costs* and *sunk costs*.

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[37]For a modern economic analysis of some aspects of the relationship between the number of firms and certain indicators of market performance, see MICHAEL L. KATZ & HARVEY S. ROSEN, MICROECONOMICS, 2nd ed. (1994): pp. 489-493.

[38] A similar point of view regarding the definition of barriers to entry is advanced by Baumol, Panzar, and Willig. They argue that ". . . unlike von Weizsäcker's, our definition seeks to specify operationally what types of impediments meet its criteria, [and] we hope to show . . . that our criterion and his overlap in substance. That is, we argue that anything that is an entry barrier by our definition does reduce the sum of consumers' and producers' surplus, while phenomena such as fixed costs and scale economies need not do so." BAUMOL, PANZAR, & WILLIG, *supra* note 23.

33. For a single-output firm, economies of scale are a consequence of enlarging the production capacity of a plant by installing higher-capacity facilities and enlarging, as necessary, the labor force necessary to produce at larger levels of output. At this higher level of output, the *average total cost of production*, i.e., the sum of *total fixed cost* plus *total variable cost*, divided by the higher level of output, is *lower* compared to the average total cost of production for smaller levels of output where the capacity of productive facilities is smaller. In general, total fixed cost ordinarily represents the estimated dollar value of the annual (implied) flow of productive services rendered by capital equipment, such as investment in cable headend and distribution facilities, that do *not* vary with small changes in the level of output.[39]

34. Achieving a lower total average cost by investing in high-capacity production facilities requires a substantial capital investment and is sometimes described as a *capital barrier to entry*. So long as *both* the incumbent and the entrant can acquire the *same* large-scale production facilities at the *same* purchase price, large total fixed costs implied by investment in high-capacity production facilities do not meet the definition of a policy-relevant barrier to entry. Implicit in the conclusion, however, is a crucial assumption that the fixed cost of high-capacity facilities cannot be reduced by reducing the level of production, *but can be eliminated by total cessation of production*. In other words, fixed cost can be eliminated by shutting down production altogether and *redeploying the capital assets* to some other production process within the firm or selling the assets to some other firm. Indeed, the incumbent may be willing to sell the capital assets to an entrant at the current opportunity cost of the assets and abandon production in this particular market.

35. If, however, the high-capacity production assets *cannot* be redeployed to some other profitable use and should the continued production of output in the existing application become unprofitable, then the fixed cost represented by the investment in such capital assets becomes a *sunk cost*. By definition, sunk costs cannot be eliminated even by total cessation of production.[40] Since sunk cost assets cannot be redeployed, *they have no opportunity cost*. As a simple example, investments in railway cars are largely a fixed cost, apart from ordinary wear and tear resulting from usage. If the current usage of a railway car between two points, A and B, becomes unprofitable, then the railroad can easily redeploy the cars to some other route. The fixed cost represented by the investment in roadbed between points A and B obviously *cannot* be redeployed and, therefore, represents a sunk cost.

36. The policy significance of the difference between fixed and sunk costs is

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[39] For a brief review of the capital theory principles that convert the price of a durable asset (a stock) into an annual price of capital services (a flow), see CARLTON & PERLOFF, *supra* note 8, Appendix 3A, pp. 77-78.

[40] *See* BAUMOL, PANZAR, & WILLIG *supra* note 23.

important.[41] While fixed costs do not ordinarily represent a policy-relevant barrier to entry, sunk costs sometimes do. Sunk costs may have a direct, and sometimes dramatic, effect on the behavior of dominant firms, such as local cable system operators. Much like the railroad track example above, the costs of constructing a cable distribution network may be viewed as sunk, where the coaxial cable plant is analogous to the roadbed investment by railroads.[42] Significant aspects of the cable distribution and video programming industries are characterized by sunk costs. As a result, strategic behavior by incumbent cable systems may be anticipated as a factor directly affecting market structure for local distribution of video programming.

37. If entry into an industry requires large sunk costs, the value of incumbency can be substantial. Incumbent systems may be able to use their incumbency to forestall or deter competitive entry via a number of entry deterring strategies.[43] In general, economic models of entry deterrence stress the inherent advantage in making the "sunk" investments *first*, thereby limiting the opportunities for profitable entry later. For example, suppose that an incumbent cable system has wired an entire franchise area. A potential entrant will realize that any large scale entry into that market will probably force price down, as the output of the entrant is absorbed by the market. Even if the costs of the entrant are as low as those of the incumbent, the post-entry price may fall below average cost, and entry will prove unprofitable.[44] If the prospective entrant's expectations match this scenario, entry is deterred. This entry-deterrent effect depends on the expectations of the entrant about post-entry

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[41] Transaction cost economics places much emphasis on *asset-specificity*, a concept logically equivalent to sunk cost, although the concept is used to explain the choice between private contracting and the internal organization of firms as alternative institutions for effectuating exchange relationships. *See* OLIVER E. WILLIAMSON, THE ECONOMIC INSTITUTIONS OF CAPITALISM (1985). *See also* Oliver E. Williamson, *Transaction Cost Economics*, HANDBOOK OF INDUSTRIAL ORGANIZATION ch. 3 (Richard Schmalensee & Robert D. Willig eds. 1989).

[42] To some extent, sunk costs are a matter of degree, since almost every asset will have some value in the second-hand market. Tirole notes that sunk investments are not an "all-or-nothing" notion; investments are sunk as long as the costs of redeploying the asset exceed the benefits from doing so. JEAN TIROLE, THE THEORY OF INDUSTRIAL ORGANIZATION 1-3 (1988).

[43] Evaluating all theories of entry deterrence where sunk costs are significant is beyond the scope of this *Appendix*. For a general review of entry deterring strategies, *see* Robert Wilson, *Strategic Models of Entry Deterrence*, 1 HANDBOOK OF GAME THEORY WITH ECONOMIC APPLICATIONS (Robert J. Aumann & Sergiu Hart eds. 1992).

[44] Albert Smiley constructs a model which simulates cable overbuilding with engineering demand and cost functions. His simulations show that profitable entry can be deterred if the incumbent wires the entire franchise market. *See* ALBERT SMILEY, *Direct Competition Among Cable Television Systems*, United States Department of Justice, Antitrust Division, EAG Paper #86-9 (1986).

behavior of the incumbent, the degree of economies of scale, and the level and nature of demand.

38. If an incumbent sets price at the monopoly level, then a prospective entrant may perceive entry to be profitable. The incumbent may be able to deter entry, however, by setting *a limit price*, i.e., a price below monopoly price but above average cost. The incumbent, by accepting less than maximum profit in the short run, prevents entry and maximizes profit in the long run.[45] The implications of a limit pricing strategy for consumer welfare are complex. Since a limit price is lower than the monopoly price, it clearly enhances consumer welfare. If the limit price is *above* the duopoly price, then potential welfare is diminished by the entry-deterring effect of the limit price. Thus, consumer welfare is directly affected by the *type* of limit pricing strategy that an incumbent cable system may adopt.[46]

2. *Product Differentiation as a Barrier to Entry*

39. In addition to sunk costs, product differentiation is sometimes viewed as an impediment to entry in local markets for multichannel video programming distribution. Incumbent cable systems may have an advantage over potential entrants arising from consumer preferences for their products. This preference might be the result of advertising, goodwill, reputation, inertia, or other factors. Product differentiation, according to Bain, is a barrier to entry as entrants must entice customers with a lower price and/or incur a greater selling expense per unit than the incumbent(s). Greater selling expenses, incurred *only* by the entrant, make product differentiation a Stiglerian barrier to entry as well.

40. Product differentiation may constitute a barrier to entry if the extent of differentiation is sufficiently "intense," i.e., consumers perceive alternative products as poor substitutes for the differentiated product or service. Intense product differentiation tends to steepen the slope of the demand curve for the differentiated product and increase the margin

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[45] This simplistic view of limit pricing fails to consider, however, the strategic reactions to entry by incumbent firms. In other words, incumbents must decide whether accommodating or opposing entry is more profitable. If the incumbent firm finds it more profitable to accommodate entry, it will reduce its output, making room for the entrant. Bain and Sylos-Labini assume that entrants expect incumbents to maintain output at pre-entry levels. *See* BAIN, *supra* note 34; PAOLO SYLOS-LABINI, OLIGOPOLY AND TECHNICAL PROGRESS (1962).

[46] Leland Johnson provides an example of a limit pricing response by a cable system when it faced competitive entry. The city of Glasgow, Kentucky, decided to build a competitive municipal cable system. Before the first mile of cable was strung, the incumbent cable operator cut its rates by 60%. This response did not discourage the municipality from continuing construction, but did send a signal to the city regarding the future profitability of its system and the competitive stance the incumbent was prepared to take. *See* LELAND JOHNSON, TOWARD COMPETITION IN CABLE TELEVISION 20 (1994).

of price over the marginal cost of production. As a result, advertising and other marketing expenditures that effectively deepen the consumer's *perception* that a product or service or certain of its attributes is unique relative to possible substitutes both preserves price-cost margins and may make it more difficult for an entrant to launch a competitive product or service. An entrant must incur promotional expenditures to overcome the incumbent's existing market dominance. Such expenditures are unrecoverable by the entrant in the event of market exit and may constitute, therefore, a sunk cost impediment to entry.

41. One view of competition in cable television holds that successful entrants must be able to sell an *identical* product, leaving price competition the only option; however, it is possible that competition in local cable markets may be enhanced by greater product differentiation. Avinash Dixit shows that entry is *easier* if two products, the incumbent's and the prospective entrant's, are *more* differentiated, i.e., poorer substitutes.[47] For example, if two goods were not considered substitutes (e.g., peanut butter and cars), then incumbent firms would have no incentive to deter entry. Interestingly, entry is more easily prevented if the incumbent can claim that its product is a good substitute for the prospective entrant's product. If the substitutability of goods enhances impediments to entry, then incumbent cable firms may be able to slow entry by expanding channel capacity, using programming proliferation to make interfirm differentiation more difficult. Thus, incumbent cable firms may increase the quantity and quality of programming in order to lower the profitability of entry, even in niche markets. If entry does occur, product differentiation will allow a firm to exploit monopoly power more effectively by "claiming a special niche for [its] product" that more closely match the diverse preferences of consumers.[48] Thus, if consumers prefer extensive variety in programming choices, entrants may find it more profitable, at least initially, to compete with the incumbent cable system by offering *complementary* rather than competitive programming.

3. Other Sources of Entry Barriers

42. Although not fully addressed in this *Report*, other impediments to market entry in local multichannel video programming distribution markets may grow in importance as competition develops. For example, the network nature of video distribution, whether over wire or air, implies the existence of *network effects* and the applicability of the *systems competition* literature.[49] If compatibility between systems becomes an issue, then barriers to

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[47] Dixit notes that the product differentiation in the Bainian sense relates to absolute differences in demand, i.e., the incumbent's level of demand is not sensitive to the entrant's price, which may still be considered a barrier to entry. In Dixit's model, product differentiation is characterized by a finite cross-price elasticity allowing the incumbent's level of demand to change with the output price of the entrant. *See* Avinash Dixit, *A Model of Duopoly Suggesting a Theory of Entry Barriers*, 9 BELL J. ECON. 20-32 (1979).

[48] *Id.*, at 29.

[49] For an overview *see* KATZ & SHAPIRO, supra note 24.

entry may arise. For example, if costly system-specific interfaces are developed, the fact that potential entrants must convince customers to switch interfaces, losing both the financial and human capital investment, may effectively impede entry.[50] These network effects are more likely to be an issue for wireless entry as system-specific receivers must be purchased by the subscriber.

43. In the *1992 Cable Act*, Congress addressed two particular policy-relevant entry barriers, namely, access to video programming and exclusive franchise contract rules. By foreclosing access to a vital input, such as cable programming, incumbent cable firms can erect a potential entry barrier that impedes or deters competitive entry. This foreclosure can occur either through the bargaining power of a large incumbent (an MSO for example), or by the downstream firm vertically integrating into the programming market and refusing to sell its programming to actual or potential rivals. Program access for multichannel video programming distributors using alternative technologies was addressed by the *1992 Cable Act* and enforcement of the rules appears successful. The local franchise process is, perhaps, the most important policy-relevant barrier to competitive entry in local cable markets.[51] Recognizing the potential barrier that franchising poses, Congress, in order to further competition in the cable industry, prohibited the "unreasonable" denial of a competitive franchise in the *1992 Cable Act*. The effectiveness of this prohibition has yet to be determined.

4. Conclusion

44. This discussion suggests that the presence of various types of sunk costs in the cable television industry probably represents policy-relevant barriers to entry in local multichannel video programming markets. As a result, entry-deterring behavior by incumbent cable systems may be anticipated as competition between cable systems and other MVPD firms develops. This *Report* does not propose, however, a policy response to this possible anticompetitive conduct at this time.

D. Sunk Costs and Industry Structure

45. The pervasiveness of sunk costs may have a decisive effect on long term industry structure.[52] Explaining the relationship between sunk costs and industry structure

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[50]The implications of compatibility in systems markets for the development of competition is addressed in the "Symposium on Compatibility," 40 J. INDUS. ECON. (March 1992).

[51] *See* Thomas W. Hazlett, *supra* note 32; Oliver Williamson, *supra* note 41; Richard Posner, *The Appropriate Scope of Regulation in the Cable Television Industry*, 3 BELL J. ECON. 98-129 (1972).

[52] A formal economic analysis of the effects of sunk costs on industry structure is provided by JOHN SUTTON, SUNK COSTS AND MARKET STRUCTURE (1992). The following discussion closely follows Sutton's conceptual approach.

depends on the distinction between *exogenous* and *endogenous sunk costs*. Exogenous sunk costs represent irreversible investments in productive capacity determined in substantial part by the current technology of production. Thus, in the cable industry, the investment in headend and local distribution facilities sufficient to serve a defined service area represents exogenous sunk costs: both the current technology of multichannel video distribution and the service requirements established by franchising authorities are exogenous factors that drive the amount of investment that a cable operator must commit to a particular multichannel video distribution market.[53] More simply, business firms in general and cable operators in particular have very limited discretion in determining the magnitude of exogenous sunk costs.

46. By contrast, endogenous sunk costs represent expenditures on inputs of production that business firms in general and cable operators in particular can vary with substantial discretion in pursuing business objectives. In general, spending on advertising and research and development are prominent examples of endogenous sunk costs. Although the firm can vary the amount of spending on such inputs of production, such spending, once made is necessarily committed to a particular purpose or business objective and cannot be costlessly redirected to some other purpose. In the cable television industry, spending on video programming is a conspicuous example of a major endogenous sunk cost: spending committed to one type of programming cannot be costlessly redeployed to another type of programming.[54]

47. The analytical significance of the distinction between exogenous and endogenous sunk costs in the cable industry is apparent if the evolution of industry structure is viewed as a *two-stage game*.[55] In the first stage of the game, a cable operator invests in a local distribution network of sufficient scale to serve subscribers in the franchised service area. These fixed *setup costs* incurred in this first stage of the game represent exogenous sunk costs.

48. The second stage of the game analyzes the nature of price competition that occurs *after* the sunk setup costs are incurred.[56] Prices for video programming services set at

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[53] From the perspective of the franchising authority, such costs are clearly endogenous. It is the perspective of the firm as a potential market entrant, however, that is critical in understanding the effects of sunk costs on market structure.

[54] Long-term contractual relationships with program packagers or suppliers rather than "spot market" transactions impart a sunk cost quality to such expenditures.

[55] Although the following discussion is derived from Sutton's game-theoretic model, only an intuitive interpretation of the formal analytics is provided.

[56] Although most local multichannel video distribution markets are presently supplied by a single cable system, this monopoly industry structure is not necessarily inevitable over the longer term, especially if policy-relevant barriers to entry are removed. Thus, price competition to varying degrees should be expected in local multichannel video distribution

the second stage of the game depend only *indirectly* on the exogenous sunk costs required to enter the market, however.[57] More specifically, setup costs influence the entry decision of potential competitors. If the exogenous sunk costs implied by market entry are not perceived as unreasonably large, then more firms will enter the market for local multichannel video programming, leading to greater price competition in the second stage of the game.

49. From this conceptual viewpoint, entry decisions of firms into local markets for multichannel video programming will be influenced by the *interplay* between the levels of setup costs in the first stage of the game and the intensity of price competition that firms face at the second stage.[58] If price competition is intense at the second stage of the game, then post-entry profits will be *lower*, all other things remaining the same, and the *fewer* will be the number of firms choosing to enter the market for local video programming. Thus, long term market structure will reflect a tension between the level of exogenous sunk costs that must be committed to enter the market -- and that must be recovered to justify entry ex-post -- and the intensity of price competition that occurs in the second stage of the game. In general, more entrants will tend to increase the intensity of price competition. Lower prices resulting from such competition will make entry less attractive, however, to still other potential entrants.[59]

50. Implicit in the foregoing analysis of exogenous sunk costs and price competition is the assumption that each entrant in the local market for multichannel video programming offers similar, or virtually homogenous, programming to its subscribers. If, however, different firms offer their subscribers substantially-differentiated programming compared to that offered by competitors, then long-term market structure may differ from that of the homogenous product case. Spending on programming is an endogenous sunk cost that a cable operator can vary to deepen the extent of product differentiation relative to the programming offered to subscribers by competitors. Other things remaining the same, increases in endogenous sunk costs may be expected to enhance the subscribers' willingness to pay for the video programming package offered by the cable operator and, thereby, weaken the extent of price competition in stage two of the game. Therefore, unlike the case of homogenous programming offered by competing cable operators, market structure may still remain relatively concentrated, notwithstanding the relatively higher level of post-entry

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markets over the longer turn, as the limited experience with cable overbuilds tends to show.

[57] *See* SUTTON, *supra* note 52, at 29.

[58] *Id.*

[59] *Id.* This relationship between the extent of market entry and the extent of price competition depends critically on the *form* of price competition that actually develops. Three possibilities are commonly cited, namely, (1) Cournot competition; (2) Bertrand competition; and (3) joint profit maximization. For further discussion, see SUTTON, *supra* note 52, chps 2 & 3. Experience in local multichannel video markets where overbuilders compete directly with incumbent cable systems appears roughly consistent with Bertrand competition.

profits that persist given the weakened level of price competition.[60]

51. This discussion illustrates in a highly simplified way how both exogenous and endogenous sunk costs may have a decisive effect on the evolution of local market structure for multichannel video programming distribution over the longer term. This analysis identifies possible trade-offs between the number of actual competitors in any local cable market and the intensity of price competition that might prevail. Implicit in the analysis is the possible influence that large market areas served by any given cable operator may have in reducing market concentration; more firms may be willing to commit to the exogenous sunk costs required to enter the market if the universe of potential subscribers is larger. As a result, the possible entry-deterring effects of vigorous price competition in the stage two game would be mitigated to some extent. Such market structure implications should help guide both the nature of inquiry and policy analysis in future reports.

III.
METHODOLOGICAL ISSUES

52. The assessment of the extent of competition in the market for the delivery of multichannel video programming may be approached from alternative perspectives. In general, the few comments received on methodology recommended that a legal and economic approach should inform the Commission's analysis and urged the Commission to take a relatively broad view of competition in this and future reports. For example, WCA would like the Commission to seek data that will permit a competitive analysis broader than the "wired" market.[61] TCI urges the Commission to adopt a dynamic approach to analyzing competition in the delivered video programming market.[62] Similarly, Time Warner states that the Commission should take a broad approach in its methodology which would consider virtually all information and entertainment media in its analysis.[63] Finally, Home Box Office ("HBO") submitted a paper by Professor Paul L. Joskow which examined various methodologies the Commission could and should adopt in studying "competition".[64] HBO and Professor Joskow urge the Commission to use "comparative institutional analysis" as a means of assessing competition, which would broadly apply the tools of modern industrial

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[60] *Id.* at 27.

[61] WCA Comments at 26-27.

[62] TCI Comments at 2-6; *see also* NCTA Reply Comments at 2.

[63] Time Warner Comments at 4-9.

[64] Paul L. Joskow, Economic Methodologies for Evaluating Competition and Performance in Video Programming and Distribution Markets (Exhibit A to HBO Reply Comments).

organization economics to this industry.[65]

53. As proposed in the Notice of Inquiry in this proceeding, a prominent methodological approach developed in the field of modern industrial organization economics is the *structure-conduct-performance (SCP) paradigm.*[66] The SCP methodological framework facilitates the systematic study of the extent of competition from a variety of viewpoints, and is broad enough to accommodate a number of more specialized approaches toward the study of competition. In a general way, the organization of this *Report* is consistent with the SCP paradigm. The Commission, however, is not adopting a specific methodology for assessing the extent of competition in markets for multichannel video programming distribution at this time. Future reports, however, may address such methodological issues at greater length and propose a general methodology that is consistent with the purposes of such studies on competition in video programming distribution markets.

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[65] *Id.* at 2-9. Comparative institutional analysis would be beneficial, Professor Joskow argues, because it would evaluate markets in the context of their basic economic characteristics; would focus on long-run consumer welfare; would be able to consider the effect of regulation on market performance; and would be flexible enough to balance "imperfections of regulation against imperfections of unregulated . . . markets." *Id.* at 9.

[66] *See* F.M. SCHERER and DAVID ROSS, INDUSTRIAL MARKET STRUCTURE & ECONOMIC PERFORMANCE ch. 1 (3rd ed. 1990); CARLTON & PERLOFF, *supra* note 8, at chs. 1 & 9; TIROLE *supra* note 42.

APPENDIX I

1. This appendix describes the q ratio calculations that appear in Section V of the main text. The q ratio, defined as the ratio of the market value of a firm to its replacement cost, is a measure of market power. The Commission discussed its properties in the *1990 Cable Report*.[1] This appendix addresses the "nuts and bolts" details of the calculations. The broad procedures used follow those used by Professor Paul MacAvoy in a 1990 submission to the Commission.[2]

2. MacAvoy used two separate techniques for calculating market value. He calculated "public" market values for a sample of "pure" cable companies (*i.e.*, companies whose sole business activity was cable television delivery). The public market value is the sum of a firm's liabilities and the value of its outstanding stock (price multiplied by number of outstanding shares). This figure may then be divided by the number of subscribers that the firm serves. Table I-1 shows 1993 public market value calculations for the four firms that the Commission identified as pure cable companies. Two of them, Adelphia and TCA, were also in the MacAvoy sample. (The other three firms in the MacAvoy sample are American TV and Communications, Falcon Cable Systems Co., and Galaxy Cablevision.)

3. The second market value concept is "private" market value. This is the subscriber-weighted average of per subscriber selling prices of cable companies during a relevant period. Table I-3 contains two such estimates, one based on twenty-four 1993 transactions and one based on six announced 1994 transactions. In each case, only cash transactions are included in the calculation, because it is difficult to determine an equivalent cash value for transactions with other components.

4. MacAvoy also employed two techniques for calculating replacement costs. The first is based solely on financial data for pure cable companies and consists of an estimate of adjusted book value of tangible assets. For each pure cable company, tangible assets are divided into net plant and other tangible assets. Net plant (*i.e.*, depreciated book value of plant) is adjusted for inflation and added to other tangible assets, and the sum is divided by the relevant number of subscribers. The inflation adjustment is based on a rough estimate of the average age of plant. The average age of plant is taken to be the difference between gross and net plant divided by current annual depreciation. That average age is multiplied by an annual inflation rate (assumed herein to be four percent) to get the percentage by which net plant must be increased to adjust it for inflation.

5. The second replacement cost method uses current construction cost estimates to derive a net plant figure. This procedure entails adjusting current construction cost per

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[1] *1990 Cable Report* ¶¶ 54-59, App. E, 5 FCC Rcd at 4997-99, 5071-82.

[2] *See* Paul W. MacAvoy, *Tobin's q and the Cable Industry's Market Power*, Comments of the United States Telephone Association in Appendix 5, *1990 Cable Report*, 5 FCC Rcd 4962 (1990) (MM Docket No. 89-600).

subscriber for depreciation to obtain net plant per subscriber. Adding this net plant figure to other tangible assets per subscriber (from the sample of four pure cable companies) yields an estimate of replacement cost per subscriber. The average ratio of net to gross plant for all cable companies in the data source (the Paul Kagan Cable Financial Databook) is used to adjust current construction costs. Table I-2 exhibits these calculations for four construction cost estimates.

6. The estimates of construction costs generally have three components. They are: (1) headend and cable plant; (2) converter box; and (3) "drop and install." This last item is the cost connecting a subscriber to the cable that passes his or her home. One of the headend and cable plant estimates comes from a paper by David Reed.[3] Reed's estimate of $962 is based on an assumed 40% cable penetration rate of homes passed. The actual penetration rate in 1993 was 63%.[4] Adjusting for this yields an estimated headend and cable plant cost of $611 per subscriber. Reed estimates the cost of a converter box at $125 and of drop and install as $50. These latter figures are also used in conjunction with the alternative cable plant and headend estimates.

7. MacAvoy's series of construction cost estimates contains one figure that excludes the drop and install component. The exclusion could be justified on the grounds that at least some cable subscribers pay a separate fee for installation rather than paying for it indirectly via the monthly service charge. To preserve some consistency with the MacAvoy procedure, the current series of construction costs contains one estimate, based on Reed's figures, that excludes drop and install. Accordingly, the "Reed 1" figure in table I-2 is 736=611+125 and the "Reed 2" figure is 786=611+125+50.

8. The other two entries in Table I-2 are labelled "MacAvoy 1" and "MacAvoy 2." They track two of MacAvoy's construction cost estimation procedures. The present calculations are based on data from a different source than MacAvoy used, but the technique is the same. MacAvoy 1 starts with estimates of new build construction costs for 1993 of $646 million and new homes passed of 1.8 million. These figures, along with the 1993 penetration rate of 63% yield an estimated cable plant construction cost of $569.66. Adding to this the converter box and drop and install figures yields $744.66. The MacAvoy 2 estimate begins with the same new build construction cost estimate and with an estimate of 54,900 miles of new plant construction for 1993. Applying an assumed 90 homes per mile and the 63% penetration rate yields an estimate of $207.53. Inclusive of converter box and drop and install, the MacAvoy 2 construction cost estimate is $382.53.

9. Table I-3 contains a series of q ratio calculations, which are also reproduced in the main text of this report. By way of comparison with MacAvoy's earlier work, it is

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[3] David P. Reed, *The Prospects for Competition in the Subscriber Loop: The Fiber-to-the-Neighborhood Approach* (presented at the Twenty-First Annual Telecommunications Policy Research Conference (September 1993).

[4] Paul Kagan Associates, Inc., MARKETING NEW MEDIA, Dec. 20, 1993, at 4.

interesting to note that his public market value per subscriber figure of $1698 is lower than the $2326 figure for the current sample of pure cable firms. By contrast, MacAvoy's private market value estimate of $2311 per subscriber is significantly higher than the $1759-$1831 range for 1993 and early 1994. With respect to replacement cost, MacAvoy's median estimate based on construction cost data was $372.50, while the current figure is $444.99. The calculations herein are thus similar to those of MacAvoy, but not precisely comparable. The current sample of pure cable firms differs from that used by MacAvoy, and the construction estimates come from different sources.

TABLE I-1
Replacement Data for Four Pure Cable Companies

	ADELPHIA	MERCOM	MULTIMEDIA	TCA Average	Weighted Average
Balance Sheet Date	March 1993	Year-End	Year-End	October 1993	
Equity (mil)	287.231	9.960	1,274.442	702.838	
Liabilities (mil)	1,818.207	29.109	768.20	162.814	
Market Value (Total Equity + Liabilities) (mil)	2,105.438	39.069	2,042.732	865.652	
Subscribers Per System	1,244,000	37,757	417,333	473,000	
Market Value per System	$1,692.47	$1,034.75	$4,894.73	$1,830.13	$2,326.28
Net Plant (mil)	398.859	17.946	240.762	106.411	
Adjusted Net Plant (mil)	449.469	22.305	290.520	125.311	
Other Tangible Assets (mil)	111.135	1.310	163.056	7.259	
Replacement Cost (mil)	560.604	23.615	453.576	132.570	
Replacement Cost Per Subscriber	$450.65	$625.45	$1,086.84	$280.27	$538.81
Other Tangible Assets Divided by Subscribers	$89.34	$34.69	$390.71	$15.35	$44.46
Q Value	3.7556	1.6543	4.5036	6.5298	4.4669

Sources: Paul Kagan Assocs., Inc., CABLE TV FINANCIAL DATABOOK, 58, 70,72, 74 (1994). Subscriber information supplied by MERCOM, Inc. CABLE TV INVESTOR, June 7, 1997, at 4.

TABLE I-2
Replacement Cost Per Sub
Based on
Construction Cost Estimates

	Gross Plant Per Sub[5]	Net Plant Divided by Gross Plant[6]	Estimates Net Plant	Other Tangible Assets[7]	Replacement Costs
Reed 1	736	.541	398.18	44.46	442.64
Reed 2	786	.541	425.23	44.46	469.69
MacAvoy 1	744.66	.541	402.86	44.46	447.33
MacAvoy 2	382.53	.541	206.95	44.46	251.41

[5] See text.

[6] PAUL KAGAN ASSOCS., INC., CABLE TV FINANCIAL DATABOOK 72 (1994).

[7] From Appendix I, Table 1.

TABLE I-3
q RATIOS

Public Market Value Divided by Adjusted Book Value (Four Firms)[8]	4.47
Public Market Value Divided by Adjusted Book Value (Two Firms Common to Current and MacAvoy Sample)[9]	4.52
Public Market Value Divided by Median Replacement Costs (Four Firms)[10]	5.23
Private Market Value (1993 Transactions) Divided by Median Replacement Cost[11]	4.11
Private Market Value (Some 1994 Transactions) Divided by Median Replacement Cost[12]	3.95

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[8] From Table 1.

[9] From Table 1, weighted average of Adelphia and TCA q ratios.

[10] From Tables 1 and 2; mediam replacement cost per subscriber, $444.99.

[11] Median replacement cost per subscriber of $444.99 from Table 2. Private Market Value of $1831.10 per subscriber based on 24 cash transactions reported in PAUL KAGAN ASSOC. INC., CABLE TV FINANCIAL DATABOOK 138 (1994).

[12] Median replacement cost per subscriber of $444.99 from Table 2. Private Market Value of $1759.49 based on six cash transactions reported in Cable World, June 27, 1994, at 1, 36.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

FCC 94-249

In the Matter of	)	
	)	
Petition for Declaratory Ruling	)	MM Docket No. 92-254
Concerning Section 312(a)(7)	)	
of the Communications Act	)	

MEMORANDUM OPINION AND ORDER

Adopted: September 28, 1994 Released: November 22, 1994

By the Commission:

Background

1. The Commission has before it two applications for review and various responses to a request for public comments. The first application for review, filed by Kaye, Scholer, Fierman, Hays & Handler ("Kaye, Scholer"), appeals the action taken by the Mass Media Bureau in Letter to Messrs. Pepper and Gastfreund, 7 FCC Rcd 5599 (1992)("Gastfreund"),[1] which declined to grant the relief sought in Kaye, Scholer's petition for declaratory ruling of July 29, 1992.[2] In that action, the Mass

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[1] Both Gillett Communications of Atlanta, Inc. ("Gillett") and Kaye, Scholer made separate requests for the Declaratory Ruling now under review. Gillett did not file an application for review, but did file comments in this proceeding.

[2] In its petition, Kaye, Scholer had requested a declaratory ruling from the Commission with respect to the following:

> whether a broadcaster may, consistent with the "reasonable access" provision of Section 312(a)(7) of the Communications Act and the "no censorship" provision of Section 315(a) of the Communications Act, "channel" into those hours when there is no reasonable risk of children being in the audience, candidate "uses" that present graphic depictions of dead or aborted and bloodied fetuses or fetal tissue.

Kaye, Scholer filed its Application for Review on September 2,

Media Bureau determined that the specific political advertisement at issue, which featured the graphic depiction of dead or aborted and bloodied fetuses or fetal tissue,[3] was not indecent under 18 U.S.C. Section 1464, and, as a result, the licensee could not channel the advertisement to the indecency "safe harbor"[4] without violating Sections 312(a)(7) and 315 of the Communications Act. (47 U.S.C. Sections 312(a)(7) and 315). Kaye, Scholer seeks review on the grounds that the Bureau's decision was not consistent with established Commission policy and precedent governing the reasonable access provisions of Section 312(a)(7) and the "no censorship" clause of Section 315(a), and that the Bureau's interpretation of Section 312(a)(7) violates the first amendment rights of broadcasters by unduly circumscribing their editorial discretion.

2. Daniel Becker filed the second application for review under consideration on December 3, 1992. He appeals an October 30, 1992, Mass Media Bureau decision which declined to rule on whether a political advertisement placed by Daniel Becker on WAGA-TV, Atlanta, Georgia, was indecent under Section 1464. The Mass Media Bureau noted that the advertisement had not yet aired, and explained that the Commission and the Bureau have declined to issue advance indecency rulings to avoid imposing prior restraints on protected speech. Letter to Daniel Becker, 7 FCC Rcd 7282 (1992). In that letter, the Bureau also stated, however, that until such time as the Commission provides definitive guidance in the area, it would not be unreasonable for a licensee to rely on a prior informal staff opinion in this area, set forth in the Letter from Chairman Mark Fowler to Hon. Thomas A. Luken, dated January 19, 1984, and conclude that Section 312(a)(7) does not require it to air, during hours outside the safe harbor, material that it reasonably and in good

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1992.

[3] These political advertisements will be referred to herein as "political advertisements containing graphic abortion imagery."

[4] The safe harbor is that period of the day during which indecent material can be aired without violating the prohibition in 18 U.S.C. Section 1464 on indecent broadcasting. Pursuant to a Congressional directive, the Commission adopted rules redefining the safe harbor as 12:00 a.m. (midnight) to 6:00 a.m., but these rules have been stayed by the courts and are now on appeal. Action for Children's TV v. FCC, 11 F.3d 170 (D.C. Cir. 1993), vacated and reh'g granted en banc, No. 93-1092, 1994 WL 50415 (D.C. Cir. Feb. 16, 1994). The Commission currently recognizes an 8:00 p.m. to 6:00 a.m. safe-harbor period, as it did following the D.C. Circuit's decision in Action for Children's Television v. FCC, 852 F.2d 1332 (D.C. Cir. 1988).

faith believes is indecent. In his application for review, Becker argues that the Commission erred in declining to render an indecency ruling in advance of the broadcast because such inaction denies a federal candidate the right to reasonable access.

3. To receive the benefit of the views of interested parties on all the issues related to political advertisements featuring graphic abortion imagery, the Commission requested public comment on the issues raised by the rulings.[5] Specifically, we sought comment on all issues concerning what, if any, right or obligation a broadcast licensee has to channel, to times when children are unlikely to be in the audience, political advertisements that it reasonably and in good faith believes are indecent. We also sought comment as to whether broadcasters have any right to channel political advertisements that, while not indecent, may be otherwise harmful to children. We invited commenters to address the proper scope of any such right to channel political advertisements that are not indecent but may be harmful to children and the standard by which the Commission should evaluate the reasonableness of the broadcasters' judgments in exercising that right.

Comments

4. Seventeen formal comments and five formal reply comments were filed in response to our request. Several of them addressed the question of the channelling of political advertisements that the licensee believes are indecent. For example, the American Civil Liberties Union ("ACLU"), Mark Johansen, and the National Right to Life Committee, Inc. ("NRLC") argue that political advertisements containing graphic abortion imagery are not indecent. Johansen contends that the determination of whether speech is indecent must be made by the Commission, not the broadcaster. He argues that such determinations prior to an advertisement's airing would not constitute an impermissible prior restraint. Several commenters express concern over the effect that denominating these advertisements as indecent would have on indecency enforcement in the non-political as well as the political arena. For example, the ACLU and Action for Children's Television, et al., ("ACT") argue that, in addition to undermining the goals of the Communications Act in fostering expanded political debate, expansion of the indecency definition to include material such as that described in the Gastfreund ruling would constitute a serious constitutional infringement by interfering with First Amendment protection of news and entertainment programming. ACT maintains that such an expanded definition of indecency would

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[5] Request for Comments, 7 FCC Rcd 7297 (1992).

result in greater uncertainty regarding what material may be considered indecent.

5. Several commenters were also concerned about permitting licensees to channel the advertisements as "harmful to minors" even if not indecent. In comments that were generally representative of this point of view, Media Access Project[6] ("MAP") argues that the no-censorship provision of Section 315 does not permit any censorship by a broadcaster based upon the content of the advertisement, and that reading Section 312(a)(7) as permitting content-based decisions would nullify Section 315. The National Right to Life Committee states that voters have a right to uncensored information concerning matters of political debate and that political speech is entitled to "super-protected status" under the First Amendment. Consequently, NRLC asserts, content-based restrictions must be justified by a truly compelling interest and be narrowly tailored to affect only that interest. The ACLU contends that the "harmful to minors" rationale is not sufficient to justify a change in the Act's reasonable access and no-censorship provisions, and would give broadcasters a license to discriminate on the basis of political ideas.

6. Proponents of channelling, on the other hand, including Spokane Television, Inc. ("Spokane"), Louisiana Television Broadcasting Corp. ("LTBC"), Gillett, Mark Van Loucks, Turner Broadcasting System, Inc., and the National Association of Broadcasters generally argue that broadcasters should be given the right to make good faith decisions regarding what is indecent or may otherwise be harmful to their audiences, and to reject or channel such advertisements to time periods when children are less likely to be in the audience.[7] Gillett argues that the Commission must balance the goal of an informed electorate with its obligation to protect children from indecent speech. Spokane contends that Congress never intended Section 315 to be used as a device to thwart licensees' obligations to comply with the other provisions of the Communications Act. LTBC notes that there is no general right of access by individuals to television stations, and that narrowly tailored restrictions which serve important governmental interests are allowed. Van Loucks and Gillett argue that broadcasters should be permitted to reject entirely advertisements that contain shocking or offensive material that the station would otherwise reject as not in the public interest.

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[6] Media Access Project filed comments jointly with the Washington Area Citizens Coalition Interested in Viewers Constitutional Rights. These parties will be referred to collectively as "MAP."

[7] Gillett would include under this discretion political spots that are racist, bigoted, or otherwise shocking.

These commenters generally agree that warnings issued prior to the airing of advertisements are insufficient to protect children.[8]

7. Regarding the scope of review to be used in evaluating a broadcaster's decision to channel an advertisement, Spokane argues that FCC review should be limited to whether the broadcaster acted reasonably. The Louisiana Television Broadcasting Corporation proposes that FCC review be limited to abuse of discretion, while Gillett believes that the burden should be on the licensee to demonstrate that the material was indecent or otherwise did not meet the station's standards.

8. In addition to the comments referred to above and in the Appendix, the Commission received approximately 1,000 letters concerning the airing of political advertisements containing graphic abortion imagery. These letters have been associated with this proceeding although some were filed after the close of the comment period. The vast majority of these letters strongly oppose the airing of political advertisements containing graphic abortion imagery at times when children are likely to be in the audience.

Discussion

9. We affirm the Mass Media Bureau's decision that the political advertisement containing graphic abortion imagery considered in the Gastfreund ruling is not "indecent" under Section 1464 as we have defined the term. However, we conclude that Section 312(a)(7), which affords federal candidates the right to purchase reasonable amounts of time, does not preclude a licensee from channelling such advertisements to times of the day when children are less likely to be in the viewing audience.[9]

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[8] Planned Parenthood Federation of America, et al., request that the Commission allow broadcast stations to refuse to air advertisements which provide private information concerning persons unrelated to a political campaign who perform family planning or abortion services, because such broadcasts are not on behalf of a candidacy, are not consistent with Congress' intent in enacting Section 312(a)(7) and incite conduct which is inconsistent with federal and state law. That question is beyond the scope of our inquiry and is not addressed herein.

[9] Section 312(a)(7) of the Act states:

> (a) The Commission may revoke any station license or construction permit --
>
> * * *
>
> (7) for willful or repeated failure to allow

Nor does such an approach violate the "no-censorship" mandate of Section 315(a) of the Communications Act.[10]

Indecency

10. The graphic depictions of aborted fetuses considered in the Gastfreund ruling are not indecent. Section 1464 of the criminal code prohibits the broadcast of "any obscene, indecent, or profane language by means of radio communications." 18 U.S.C. Section 1464. The Commission has defined the term "indecent" to mean "language or material that, in context, depicts or describes, in terms patently offensive as measured by contemporary community standards for the broadcast medium, sexual or excretory activities or organs."[11]

11. While the record in this proceeding suggests that many viewers find the images of aborted fetuses deeply disturbing and patently offensive, that is not the test for indecency. Material may be shocking or outrageous, but it is not indecent within our definition unless it depicts or describes "sexual or excretory activity or organs." However disturbing, aborted fetuses or fetal tissue, alone, cannot be considered "excretory by-products" within the meaning of the indecency definition. The Bureau noted in its initial ruling that "[n]either the expulsion of fetal tissue nor fetuses themselves constitutes 'excrement.'" Id. We agree. Although some parties have suggested that the Commission's reliance upon the definition of "excrement" is a "semantic word game," that contention is simply unpersuasive, as is the contention that the term "excretory function," as set out in Pacifica, is broad enough to encompass the products of

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> reasonable access to or to permit purchase of reasonable amounts of time for the use of a broadcasting station by a legally qualified candidate for Federal elective office on behalf of his candidacy.

[10] Section 315 provides, in pertinent part:

> (a) If any licensee shall permit any person who is a legally qualified candidate for any public office to use a broadcasting station, he shall afford equal opportunities to all other such candidates for that office in the use of such broadcasting station: Provided, That such licensee shall have no power of censorship over the material broadcast under the provision of this section . . . .

[11] Infinity Broadcasting Corporation of Pennsylvania, 2 FCC Rcd 2705 (1987), aff'd in relevant part, Action for Children's Television v. FCC, 852 F.2d 1332 (D.C. Cir. 1988).

abortion. We agree with the Bureau's conclusion that "excretory functions" should be equated to scatological references. To the extent that petitioners suggest we should expand our definition of indecency, we choose not to do so.[12] To expand the term "excretory function" or the concept of indecency to include the secretion of any bodily fluid or material would deprive the definition of any meaningful limit. Such an expanded definition arguably would encompass televised scenes of a character sweating, blowing his nose, or dressing a wound, and would be far afield from the Commission's or the Court's concerns in Pacifica. See, e.g., Comments of the American Civil Liberties Union at 5-6.[13]

12. Even if the material at issue in the Gastfreund ruling could be considered indecent under some meaning of that term, the images cannot be divorced from the context of a political campaign. As we have previously stressed, to determine whether particular material is indecent, we look "first and foremost to the context in which language was presented - a review that encompasses a host of variables, including, among other things, an assessment of whether the language was used in a 'shocking' or 'vulgar' fashion or was without merit." Letter to Peter Branton, 6 FCC Rcd 610 (1991), aff'd sub nom. Branton v. FCC, 993 F.2d 906 (1993), cert. denied, 114 S. Ct. 1610 (1994); Infinity Broadcasting Corporation of Pennsylvania, 2 FCC Rcd 2705 (1987), aff'd in relevant part, Action for Children's Television v. FCC, 852 F.2d 1332 (D.C. Cir. 1988), King Broadcasting Co., 5 FCC Rcd 2971 (1990). The Commission's analysis of context has always encompassed more than just the four corners of the material being reviewed. The advertisement in Gastfreund that prompted this inquiry was presented in the context of a political campaign and it is beyond dispute that the issue of abortion is an important question in American politics. Accordingly, the context in which the advertisement at issue was presented provides further support for our conclusion that it was not indecent. Cf. Letter to

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[12] We remain of this view notwithstanding that a district court in Georgia concluded that a videotape depicting "the actual surgical procedure for abortion" was indecent. Gillett Communications v. Becker, 807 F. Supp. 757, 763 (N.D. Ga. 1992), appeal dismissed mem., 5 F.3d 1500 (11th Cir. 1993). In our view, however, the district court erroneously applied the indecency standard in that case.

[13] Nor does abortion fall within Pacifica's definition of "sexual activity." It is not reasonable, for example, to conclude that the advertisements in question are indecent on the theory that "abortions and fetuses are related to sex and reproduction." Mangan, Aborting the Indecency Standard in Political Programming, 1 Communications Law CONSPECTUS 73, 83(1993). This would suggest that any byproduct of sex - arguably all of life - is indecent.

William T. Carroll, Esq. (Christian Action Network), FCC Ref. No. 8210-AJZ, 920504 (MMB, June 12, 1992).

Channelling

13. But this is not the end of our inquiry. Licensees have asked us to confirm that even if political advertisements are not indecent, the Act does not prevent licensees from channelling such advertisements that show aborted fetuses or similar depictions to times when unsupervised children are less likely to be in the audience. In the Request for Comments, we thus asked "whether broadcasters have any right to channel material that, while not indecent, may otherwise be harmful to children." 7 FCC Rcd at 7297. We conclude that a licensee's exercise of such discretion is compatible with the obligation to permit federal candidates to purchase reasonable amounts of time pursuant to Section 312(a)(7) and the prohibition of censorship in Section 315(a).

14. While this is a matter of first impression for the Commission, we note that our prior treatment of Section 312(a)(7) supports this result. In particular, the Commission has made clear that Section 312(a)(7) does not entitle a federal candidate "to a particular placement of his or her political announcement on a station's broadcast schedule." Commission Policy in Enforcing Section 312(a)(7) of the Communications Act, 68 F.C.C.2d 1079, 1091 (1978). Further, although the Commission's general policy is to require that federal candidates must have access to "a wide array of dayparts and programs," we have long recognized that "there may be circumstances when a licensee might reasonably refuse broadcast time to political candidates during certain parts of the broadcast day."[14]

15. We already have concluded that Section 312(a)(7) does not preclude licensees from considering the potential impact of political advertisements on their audience in making access decisions. We have a longstanding policy, for example, of allowing broadcasters to deny access by political advertisers to newscasts. See, e.g., Law of Political Broadcasting and Cablecasting: A Political Primer, 100 F.C.C.2d 1476, 1525 (1984). We recently reaffirmed this policy on the grounds that broadcaster discretion "serve[s] the public interest by

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[14] Codification of the Commission's Political Programming Policies, 7 FCC Rcd 678, 682 (1991), quoting Commission Policy in Enforcing Section 312(a)(7) of the Communications Act, 68 F.C.C.2d 1079, 1091 (1978).

preserving the journalistic integrity . . . in this vital area of programming." Codification of the Commission's Political Programming Policies, 7 FCC Rcd 678, 682 (1991), reconsidered in part, 7 FCC Rcd 4611 (1992). Our experience has been that some broadcasters permit political advertisements during newscasts and others do not. The decision is left to the licensee, based on its news and editorial policies.

16. Likewise, we believe that nothing in Section 312(a)(7) precludes a broadcaster's exercise of some discretion with respect to placement of political advertisements so as to protect children. There is evidence in this record indicating that the graphic political advertisements at issue can be psychologically damaging to children. See Comments of Mark Van Loucks at Exhibit C; see also Gillett Communications of Atlanta, Inc. v. Becker, 807 F. Supp. at 757. The public interest standard of the Act clearly contemplates that appropriate measures may be taken to protect the well-being of children, as reflected in the provisions relating to broadcast indecency, as well as policies regarding commercials directed at children and the obligation of broadcasters to air instructional and informational programming for children.[15] Accordingly, we are unwilling to infer that Congress, in affording federal candidates a limited statutory right to purchase reasonable amounts of broadcast time, intended to strip licensees of all discretion to consider the impact of political advertisements featuring graphic depictions of abortions on children in their audience.

17. In reaching this decision, we are also mindful that the statutory scheme of the Act generally envisions that "[o]nly when the interests of the public are found to outweigh the private journalistic interests of broadcasters will government power be asserted within the framework of the Act." CBS, Inc. v. DNC, 412 U.S. at 110. Therefore, to the extent broadcasters exercise their discretion in a manner that comports with Section 312(a)(7), Section 315(a), and the public interest standard of the Act, we believe their actions are permissible.

18. In considering broadcaster compliance with Section 312(a)(7), and as reflected in our longstanding policies implementing that Section, licensees as a general matter are not permitted to impose blanket bans on federal candidate access to the types, lengths and classes of time which they sell to commercial advertisers. 1978 Policy Statement, 68 F.C.C. 2d at 1090. Consistent with that policy, licensees must give reasonable and good faith attention to access requests on an

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[15] See Children's Television Act of 1990, Pub. L. No. 101-437, (codified at 47 U.S.C. 303a (Supp. 1992)).

individualized basis. Therefore, any decision to channel must be based on the reasonable, good faith judgment of the broadcaster that political advertisements containing graphic abortion imagery should not be aired when there is a reasonable risk that large numbers of children may be in the audience. Such a decision necessarily requires an individualized assessment as approved in CBS, Inc. v. FCC, 453 U.S. 367, 387 (1981). Further, in making that assessment, licensees must carefully balance federal candidates' specific time requests against factors relating to the protection of children in the audience.

19. We emphasize that we do not require -- nor do we encourage -- licensees to channel political advertisements containing graphic abortion imagery. Rather, we leave that decision to the reasonable, good faith judgment of broadcasters. We conclude only that licensees may consider any such advertisement's impact on children in making access decisions under Section 312(a)(7).

20. The discretion of a licensee that chooses to channel a political advertisement is also limited in light of Section 312(a)(7)'s purpose to promote political expression. Section 312(a)(7) makes a significant contribution to freedom of expression. See CBS, Inc. v. FCC, 453 U.S. at 396. If licensees do channel, therefore, they are expected to provide access to times with as broad an audience potential as is consistent with the federal candidate's right to reasonable access.[16] This is consistent with our general policy under Section 312(a)(7) that licensees should afford access to federal candidates in prime time, when access to voters is greatest. 68 F.C.C. 2d at 1090.

21. Finally, a broadcaster's decision to channel an advertisement "may not be invoked as [a] pretext[] for denying access." CBS, Inc. v. FCC, 453 U.S. at 387. A licensee who chooses to channel political advertisements containing graphic abortion imagery cannot do so out of disagreement with the candidate's political position. The licensee's discretion should relate to the nature of the graphic imagery in question and not

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[16] In his application for review, Daniel Becker contends that our policy of refusing to make indecency rulings in advance of broadcast will allow the channelling of ads to time periods with minimal viewership, thereby violating Section 312(a)(7). As indicated above, licensees may not engage in channelling that would deny a federal candidate's right to reasonable access. We therefore find no reason to change our policy of declining to make advance rulings considering indecent programming.

to any political position the candidate espouses.[17]

22. This policy, we believe, fully complies with the "rule of reason" embodied in Section 312(a)(7) and properly balances relevant public interest considerations, including the First Amendment values inherent in the Act. We note in this regard that candidates have no First Amendment right of access to broadcast stations for the purpose of engaging in political speech. See Kennedy for President Committee v. FCC, 636 F.2d 417, 431 (D.C. Cir. 1980). Rather, in broadcasting, it is the First Amendment right of viewers and listeners that is paramount. Id. The public's right to have access to political speech is not impeded by this policy. As noted, licensees who choose to channel political advertisements containing graphic abortion imagery they believe are harmful to children must air those advertisements in time periods in which the audience potential is broad enough to meet their reasonable access obligations. Nor may licensees discriminate among candidates based on a candidate's position on the issues.

23. At the same time, by leaving undisturbed a reasonable measure of private, journalistic discretion, licensees are able to consider and balance candidate needs in relation to the special needs of children in their viewing audience. So long as the limited, statutory right of reasonable access for federal candidates is ensured under this policy -- and we believe it is -- we see no reason based on constitutional or other principles to depart from the Act's overriding design which relies in the first instance on the good faith discretion of private broadcast licensees. That fundamental policy of the Act to rely on broadcasters to balance the public's sometimes competing informational needs and interests also significantly furthers First Amendment principles by avoiding government involvement in access issues. See CBS, Inc. v. DNC, 412 U.S. at 126-27; Kennedy for President Committee v. FCC, 636 F.2d at 432.

24. Finally, broadcasters' limited exercise of discretion in this area would not, as some commenters suggest, violate the no-censorship provision of Section 315(a). That section, which governs "uses" of broadcast stations by political candidates, states that licensees "shall have no power of censorship over the material broadcast under [this] provision." 47 U.S.C. Section

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[17] See, e.g., Henry Geller, 95 F.C.C.2d at 1241-42. In the context of news programming exemptions under Section 315(a), broadcasters' choices are evaluated on their news judgment and their lack of intent to engage in favoritism. With respect to graphic abortion advertisements, we would examine the licensee's good faith belief that the material in question could harm the children that may be in the audience as well as any evidence of favoritism.

315(a). Since 1948, the Commission consistently has held that this requirement bars licensees from removing potentially defamatory statements from political spots. Farmers Educational and Cooperative Union of America, North Dakota Division v. WDAY, 360 U.S. 525, 528 (1959)(censorship connotes examination of thought in order to prevent publication or to alter, affect, or control the subject matter of the broadcast). In upholding the statute, the Supreme Court pointed out that "permitting a broadcasting station to censor allegedly libelous remarks would undermine the basic purpose for which Section 315 was passed -- full and unrestricted discussion of political issues by legally qualified candidates." Id. at 29. We fully agree that permitting broadcasters to alter the content of political ads to avoid libel suits would violate the mandate of Section 315. But that is not the situation presented by this Inquiry. We are not granting licensees the ability to delete political statements. We are simply recognizing that a licensee may, consistent with its public interest obligations, channel political advertisements containing graphic abortion imagery to times when, although consistent with its obligation to provide reasonable access, the likelihood that children will be in the audience is diminished. This added measure of licensee discretion does not constitute "censorship" as that term is used in the Communications Act.[18]

Conclusion

25. Based on the foregoing, and pursuant to Section 1.115(g) of the Commission's rules, the Bureau's ruling in Letters to Messrs. Pepper and Gastfreund IS MODIFIED for the reasons stated above; Kaye, Scholer's Application for Review IS GRANTED to the extent set forth herein and denied in all other respects; and Daniel Becker's Application for Review IS DENIED.[19]

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

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[18] See also FCC v. Pacifica Foundation, 438 U.S. 726, 735 and n.9 (1978)(prohibition against censorship in Section 326 denies the Commission "any power to edit proposed broadcasts in advance and to excise material considered inappropriate . . . .")

[19] On March 26, 1993, Gillett filed a Request to Reopen the Record on the above proceeding. Because of this action, however, Gillett's Request is now moot.

APPENDIX

FORMAL COMMENTS

American Civil Liberties Union

Daniel Becker

Gillett Communications of Atlanta, Inc.

Joint Comments of the Action for Children's Television Association of Independent Television Stations, Capital Cities/ABC, Inc., Fox Television Stations, Inc., Greater Media, Inc., Infinity Broadcasting Corporation, National Association of Broadcasters, National Broadcasting Company, National Public Radio, People for the American Way, Post-Newsweek Stations, Inc., Public Broadcasting Service, Radio-Television News Directors Association, The Reporters Committee for Freedom of the Press, and Society of Professional Journalists

KXAN-TV

Larson For Life U.S. Senate Committee

Louisiana Television Broadcasting Corp.

Mark Johansen

Mark Van Loucks

Media Access Project and the Washington Area Citizens Coalition Interest in Viewers' Constitutional Rights

Michael Bailey

National Association of Broadcasters

National Right to Life Committee, Inc.

Planned Parenthood Federation of America, Inc., Planned Parenthood of the Rocky Mountains, and Planned Parenthood of Greater Iowa

Senator Byron L. Dorgan

Spokane Television, Inc.

Before the
Federal Communications Commission FCC 94-256
Washington, D.C. 20554

In the Matter of	)	
	)	
Simplification of the	)	CC Docket No. 92-296
Depreciation Prescription	)	
Process	)	

Further Order Inviting Comments

Adopted: October 7, 1994 **Released:** October 11, 1994

Comment Date: November 14, 1994

Reply Comment Date: December 14, 1994

By the Commission:

I. INTRODUCTION

1. On September 23, 1993, we adopted streamlined depreciation prescription procedures for the local exchange carriers ("LECs") regulated under our price cap incentive regulatory plan.[1] These procedures require us to establish ranges for the future net salvage and projection life estimates that are used to compute depreciation rates for plant categories.[2] The new procedures generally permit price cap LECs to make streamlined filings for changes in depreciation rates for these categories, as long as these estimates fall within the prescribed ranges. In our Second

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[1] Simplification of the Depreciation Prescription Process, Report and Order, 8 FCC Rcd 8025 (1993) (Depreciation Simplification Order).

[2] Rates are determined by a depreciation rate formula:

$$\text{Depreciation Rate} = \frac{100\% - \text{accumulated depreciation}\% - \text{future net salvage}\%}{\text{average remaining life}}$$

This formula requires forecasting two parameters: future net salvage (FNS) and average remaining life (ARL). The FNS is the estimated gross salvage of the plant less any estimated cost of removal. The ARL is the estimated average of the future life expectancy of investment in a particular plant account. The ARL is derived from two basic factors: a projection life and a survivor curve. The projection life is the life expectancy of new additions to plant, whereas the survivor curve describes the percentage of plant investment surviving at each age that the plant is in service. Id. at 8030.

Report and Order,[3] we adopted underlying factor ranges for 22 depreciation rate categories. By this Further Order Inviting Comments, we invite comments on our proposals for setting ranges for the remaining 12 plant categories.

II. BACKGROUND

2. Prior to adoption of the Depreciation Simplification Order, the depreciation prescription process required carriers to submit extensive data to support the underlying depreciation basic factors that are the future net salvage, projection life, and survivor curve estimates used to compute proposed depreciation rates.[4] These data requirements often resulted in voluminous submissions, consisting of up to 25 pages of analysis for each of 34 plant categories. In recognition of the regulatory, technological, and market changes that price cap LECs face, we decided to simplify the process by establishing ranges that specify maximum and minimum amounts for two of the basic depreciation factors, the future net salvage and projection life estimates.[5] Under our new process, if a price cap LEC meeting the requisite criteria[6] selects future net salvage and projection life estimates that are within the established ranges, it need not submit the detailed supporting data otherwise required.[7] In addition, under the new procedures, price cap LECs can change these basic factors annually, as opposed to the current triennial represcription cycle.[8] These streamlined procedures are intended to simplify the depreciation process, achieve administrative savings, and allow the price cap LECs greater flexibility in the depreciation process, while continuing an appropriate oversight of their depreciation rates.[9]

3. We determined that the new, streamlined procedures should be implemented in two phases, beginning with the accounts most readily adaptable to the range approach. We have

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[3] Simplification of the Depreciation Prescription Process, Second Report and Order, 9 FCC Rcd 3206 (1994).

[4] See Simplification of the Depreciation Prescription Process, Notice of Proposed Rulemaking, 8 FCC Rcd 146, 147 (1993).

[5] Depreciation Simplification Order, 8 FCC Rcd at 8026.

[6] There are two prerequisites for using the streamlined procedures. First, the basic factors underlying the price cap LEC's current depreciation rate for an account must be within the established ranges. If the basic factors are not within the established ranges, the price cap LEC must submit a full depreciation study to move the basic factors within the established ranges before it can use the streamlined procedures. Second, the basic factors proposed to be used for a new depreciation rate must also be within the established ranges. Id. at 8054-55.

[7] Id. at 8035, 8054-55. We delegated to the Common Carrier Bureau the authority to determine the filing requirements for range accounts consistent with our decision Id. at 8054, n.129.

[8] Id. at 8054.

[9] Id.

completed phase one of the streamlining process and adopted ranges for 22 plant categories.[10] We now begin phase two by proposing ranges for eight of the remaining categories. If we implement these proposals, we will have established ranges of projection life and future net salvage factors for 30 of the 34 plant categories. These plant categories represent 85% of the total plant investment. In addition, we propose in this notice alternate simplified procedures for the other four accounts. We solicit public comment on the following proposals for phase two.

III. DISCUSSION

A. Accounts For Which Ranges Are Proposed

4. We propose to establish ranges for eight of the remaining twelve plant categories. (See Appendix). In the Depreciation Simplification Order, we set forth a number of specific data that should be considered in establishing the projection life and future net salvage ranges,[11] and we used these data to formulate the ranges listed in the attached Appendix. For each plant category, we first developed a range of one standard deviation from the mean of each of the projection life and the future net salvage basic factors underlying the currently prescribed LEC depreciation rates. We then determined whether there are technological trends or recent changes in carrier investment plans that might not be fully reflected in the LECs' prescribed factors. Finally, we considered the number of LECs with basic factors that fall within the initial ranges and altered the ranges where appropriate. We recognized, however, that these specifically enumerated data must be considered in light of our obligation to prescribe reasonable depreciation rates:

> we wish to make the ranges wide enough to accommodate a significant number, if not all, of the LECs. On the other hand, we must not make the ranges so wide that they would no longer enable us to exercise effective oversight of depreciation rates.[12]

Thus, in developing the proposed ranges, we considered both the specific data enumerated in the Depreciation Simplification Order and our overriding responsibility to prescribe reasonable depreciation rates. We set forth in the Appendix our proposed projection life and future net salvage ranges for these eight plant categories.

B. Four Accounts For Which Ranges Are Not Proposed

5. We do not propose to establish ranges for Account 2211, Analog Electronic Switching;[13]

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[10] See Second Report and Order, 9 FCC Rcd at 3211.

[11] Id. at 8050.

[12] Id. at 8049.

[13] 47 C.F.R. §32.2211.

Account 2215, Electro-mechanical Switching;[14] and Account 2431, Aerial Wire.[15] These are "dying accounts"[16] as LECs are replacing the plant in these accounts with newer technologies. The LECs are rapidly phasing out this obsolete equipment in accordance with specific retirement schedules that are based on company plans to modernize their networks.[17] Depreciation rates for this equipment can be readily calculated from these retirement schedules. We believe that depreciation rates for such equipment that are based upon a LEC's specific retirement plans are more accurate than rates based upon national averages. Moreover, the calculations are less complicated than those for other plant accounts, since detailed statistical analyses are not required to forecast lives.

6. In addition, we do not propose to set ranges for Account 2121, Buildings.[18] For depreciation study purposes, we have permitted the LECs to subdivide this account and estimate lives for each subcategory. Moreover, we allowed the LECs flexibility to develop individual methods of categorization. As a result, some LECs subdivided this account based on the size of the buildings, some by location, and others based on use. Because of the significant differences among the categorization methods, the LECs' current basic factors for the subaccounts cannot be used to establish nationwide ranges. If ranges are to be developed for the buildings account, the LECs' data must be recast into new, uniform subcategories.

7. We believe that the cost of establishing such subcategories would outweigh the benefits. The LECs have indicated that the cost of compiling the information necessary to develop new subcategories would be substantial.[19] Moreover, the LECs do not have plans to add or retire a significant number of buildings in the next few years. As a result, the underlying depreciation factors applicable to Account 2121 likely will not change, and an extensive analysis of the buildings account probably will not be necessary within the next few years. Accordingly, we propose to maintain the basic factors underlying the currently prescribed depreciation rates for

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[14] 47 C.F.R. §32.2215.

[15] 47 C.F.R. §32.2431.

[16] "Dying accounts are asset accounts in which little or no new investment is being made, and for which substantial retirements are impending." Amortization of Depreciation Reserve Imbalances of Local Exchange Carriers, Report and Order, 3 FCC Rcd 984, 990 n.10 (1988).

[17] For example, both Ameritech-Illinois and Bell Atlantic-New Jersey have already retired all of their electro-mechanical switching equipment. See Illinois Bell Telephone Company 1991 Depreciation Rate Study (November 15, 1990); New Jersey Bell Telephone Company 1991 Depreciation Rate Study (May 7, 1991). In addition, Ameritech-Illinois and Bell Atlantic-New Jersey plan to retire all of their analog electronic switching equipment by 1997 and 1998, respectively. See Ameritech-Illinois 1994 Depreciation Rate Study (April 26, 1994); Bell Atlantic-New Jersey 1994 Depreciation Rate Study (May 10, 1994).

[18] 47 C.F.R. §32.2121.

[19] See Letter from Thomas R. Whittaker, Chairman, United States Telephone Association Ad Hoc Depreciation Committee, to Ms. Fatina Franklin, Chief, Depreciation Rates Branch (June 21, 1994).

the buildings account, until our three-year range review when we will reconsider whether ranges would be appropriate for this account.[20] In the interim, we believe that the data required under the streamlined procedures will be adequate, and we propose to require that the price cap LECs provide only these data for the buildings account.

IV. PROCEDURAL MATTERS

A. Ex Parte

8. This is a non-restricted notice and comment rulemaking proceeding. Ex Parte presentations are permitted, except during the Sunshine Agenda period, provided they are disclosed as provided in the Commission's rules.[21]

B. Regulatory Flexibility

9. We certify that the Regulatory Flexibility Act of 1980 does not apply to this proceeding because if the proposals in this Order Inviting Comments are adopted, there will not be a significant economic impact on a substantial number of small business entities, as defined by Section 601(3) of the Regulatory Flexibility Act.[22] Because of the nature of local exchange and exchange access service, the Commission has concluded that small telephone companies are dominant in their fields of operation and therefore are not "small entities" as defined by that Act.[23] The Secretary shall send a copy of this Order Inviting Comments, including this certification, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with Section 603(a) of that Act.[24]

V. COMMENT DATES

10. We invite comment on the proposals set forth above. Pursuant to applicable procedures set forth in Sections 1.415 and 1.419 of the Commission's Rules,[25] interested parties may file comments on or before November 14, 1994, and reply comments on or before December 14, 1994. To file formally in this proceeding, interested parties must file an original and four copies of all comments and reply comments. If commenters want each Commissioner to receive a personal copy of their comments, they must file an original plus nine copies. Interested parties

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[20] See Depreciation Simplification Order, 8 FCC Rcd at 8058.

[21] See generally 47 C.F.R. §§ 1.1202, 1.1203, 1.1206(a).

[22] 5 U.S.C. §601(3).

[23] See MTS and WATS Market Structure, 93 FCC 2d 241, 338-39 (1983).

[24] 5 U.S.C. §603(a).

[25] 47 CFR §§ 1.415, 1.419.

should send comments and reply comments to Office of the Secretary, Federal Communications Commission, Washington, D.C. 20554. Parties should also file one copy of any documents filed in this docket with the Commission's copy contractor, International Transcription Services, Room 246, 1919 M Street, N.W., Washington, D.C. 20554. We also ask that parties send a courtesy copy of their comments to the Accounting and Audits Division, 2000 L Street, N.W., Washington, D.C. 20036. Comments and reply comments will be available for public inspection during regular business hours in the FCC Reference Center (Room 239) of the Federal Communications Commission, 1919 M Street, N.W., Washington, D.C. 20554.

VI. ORDERING CLAUSE

11. Accordingly, IT IS ORDERED, pursuant to Sections 1, 4(i), 4(j), and 220(b) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 154(j), and 220(b), that NOTICE IS HEREBY GIVEN of proposed plant accounts for which basic factor ranges should be established and the ranges proposed for those accounts to be used in the depreciation prescription process as described in the Depreciation Simplification Order.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

APPENDIX

PROPOSED ACCOUNTS AND RANGES

ACCOUNT NUMBER	ACCOUNT NAME	DEPRECIATION RATE CATEGORY	PROJECTION LIFE RANGE (YEARS)		FUTURE NET SALVAGE RANGE (PERCENT)	
			LOW	HIGH	LOW	HIGH
2220	Digital switching	Digital Switching	16	18	0	5
2220	Operator systems	Combined	8	12	0	5
2232	Circuit equipment	Digital	11	13	0	5
2411	Poles	Poles	25	35	-75	-50
2421	Aerial Cable	Metallic	20	26	-35	-10
2423	Buried Cable	Metallic	20	26	-10	0
2426.	Intrabuilding network cable	Metallic	20	25	-30	-5
2426	Intrabuilding network Cable	Non-metallic	25	30	-15	0

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)
	)
Cincinnati Bell Telephone	)
Company Petition for Waiver	)
of Section 24.204 of the	)
Commission's Rules	)

ORDER

Adopted: November 1, 1994; Released: November 3, 1994

By the Commission:

I. INTRODUCTION AND BACKGROUND

1. The Cincinnati Bell Telephone Company ("CBT") has petitioned for waiver of the PCS/cellular cross-ownership rule contained in Section 24.204 of our rules so that CBT may bid on and obtain a license in the broadband Personal Communications Service ("PCS") for more than 10 MHz of spectrum in the same geographic market where it has attributable cellular holdings. That rule prohibits entities with an attributable ownership interest in a cellular licensee (*e.g.* partnership and other ownership interests amounting to 20 percent or more of a cellular licensee) from obtaining a 30 MHz broadband PCS license if the populations of the respective cellular and PCS license areas overlap significantly (*i.e.*, if the PCS license is "in-market").[1] At the time CBT's petition was filed, the rules provided that parties with holdings in certain cellular licensees (*i.e.*, those covering 20 percent or less of the PCS service area population) could participate in auctions for more than 10 MHz of PCS spectrum. As discussed below, this rule was expanded recently to allow parties with non-controlling interests to participate in 30 MHz broadband PCS auctions.[2]

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[1] *See* 47 C.F.R. § 24.204.

[2] *See Amendment of the Commission's Rules to Establish New Personal Communications Services*, GEN Docket No. 90-314, Third Memorandum Opinion and Order, FCC 94-265 (released October 19, 1994) at paras. 33-34 ("*Broadband PCS Reconsideration Order*").

2. CBT currently has approximately a 45 percent limited partnership interest in the Cincinnati SMSA Limited Partnership ("Partnership"), an entity formed under Delaware partnership law that holds cellular licenses covering a geographic area that includes the cities of Cincinnati, Columbus and Dayton, Ohio.[3] Ameritech Mobile Phone Service of Cincinnati, Inc. ("Ameritech"), has approximately a 53 percent interest in the Partnership and is the general partner.[4] CBT has initiated a proceeding in the Delaware Court of Chancery to dissolve the Partnership, an action that Ameritech apparently is contesting.[5] Regardless of the outcome of that proceeding, CBT seeks a waiver of Section 24.204 to the extent necessary to enable CBT to retain its interest in the Partnership, participate in the auction of 30 MHz in-market PCS licenses and, assuming it is the winning bidder, to hold such a license.

3. In response to petitions seeking further reconsideration of our broadband PCS service rules established in GEN. Docket No. 90-314, we concluded that entities with attributable, but non-controlling cellular interests like CBT's will be permitted to bid on in-market 30 MHz PCS licenses.[6] Since Section 24.204 no longer bars CBT from participating in the auction of such licenses, the aspect of its waiver request that addresses its participation in the auction is moot.[7]

4. In this order, we deny CBT's request to retain its interest in the Partnership and unconditionally hold an in-market 30 MHz PCS license. As explained hereafter, however, we will grant CBT an extension of the post-auction divestiture time period to allow CBT a limited amount of additional time to divest its partnership interest to come into compliance with the PCS/cellular cross-ownership rule, if it obtains a PCS license.

II. POSITIONS OF THE PARTIES

5. CBT and Ameritech are the only parties to this proceeding. In response to a Public Notice seeking comment on

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[3] *See* CBT Petition at 2.

[4] *Id.*

[5] *See* CBT Addendum to Petition for Waiver, filed September 16, 1994 ("CBT Addendum").

[6] *See Broadband PCS Reconsideration Order* at paras. 33-34.

[7] As a result, we will not discuss the portions of the record pertaining to that aspect of the CBT Petition.

CBT's petition and an addendum to that filing,[8] Ameritech filed comments on September 26, 1994, and CBT replied on October 3, 1994.

6. CBT contends that the bar on cross-ownership of attributable, in-market cellular and PCS interests is arbitrary and unreasonable as applied to CBT because its investment in the Partnership is a passive, non-controlling interest. CBT alleges that an interest of this nature precludes CBT from engaging in the kinds of anticompetitive conduct that Section 24.204 is designed to prevent.[9] CBT adds that the Commission has adopted "more realistic" attribution standards in other situations, including a higher standard for restricting designated entities' eligibility to bid in entrepreneurs blocks,[10] and for determining cognizable interests in the broadcast context.[11] CBT claims its non-controlling interest in the Partnership would not limit its participation in the broadband PCS auction if either of these standards were applied.[12]

7. CBT states that it is seeking dissolution of the Partnership in Delaware Court of Chancery "because of the Partnership's woeful financial performance."[13] CBT further states, however, that on September 9, 1994, the Delaware court denied CBT's request to try separately the counts seeking the dissolution remedy prior to the first broadband PCS auction, which is scheduled to be held December 5, 1994.[14] CBT contends that absent dissolution of the Partnership, the partnership agreement makes voluntary withdrawal from the Partnership by CBT

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[8] The Public Notice also specified the ex parte rules that govern this proceeding. *See* PUBLIC NOTICE, Commission Applies "Permit But Disclose" Ex Parte Rules to Cincinnati Bell Telephone Petition for Waiver, Cellular Eligibility Rules (Section 24.204), Comment Dates Set, Mimeo No. 44825, Sept. 19, 1994.

[9] CBT Petition at 4-5.

[10] See Implementation of Section 309(j) of the Communications Act (Competitive Bidding), PP Docket No. 93-253, Fifth Report and Order, FCC 94-178, July 15, 1994 (para. 160) ("*Fifth Report and Order*"), petitions for reconsideration pending; 47 C.F.R. §§ 24.709, 24.720.

[11] See 47 C.F.R. §73.3555 and notes.

[12] CBT Petition at 5-6.

[13] CBT Addendum at 2.

[14] *Id.*

"financially punitive" because the agreement limits CBT to a distribution equal to its current capital account unless a willing buyer is found and Ameritech agrees to accept the buyer as its partner.[15] CBT alleges that under these circumstances it has been unable to procure a willing purchaser for its 45 percent interest.

8. Ameritech states that CBT's allegations respecting the financial performance of the Partnership are unsupported and, in any event, do not provide adequate basis for waiver. Ameritech argues that we have considered and rejected CBT's arguments respecting broadband PCS license eligibility standards several times in our PCS rulemaking, and that the CBT Petition contains no argument that would support a waiver of the general rule.[16] CBT replies that Ameritech's comments illustrate CBT's difficulties as a non-controlling limited partner. CBT also opposes Ameritech's proposal, submitted in its September 14, 1994 reply comments filed in the PCS rulemaking, that parties with cellular interests precluding their participation in the broadband PCS auction be permitted to divest those interests to an independent trustee prior to the auction.[17] CBT states that Ameritech's proposal would leave CBT's pre-auction divestiture subject to Ameritech's approval under the partnership agreement.

III. DISCUSSION

9. Waiver of a Commission Rule is appropriate only if (1) the underlying purpose of the rule will not be served, or would be frustrated, by its application in a particular case, and grant of the waiver is otherwise in the public interest, or (2) unique facts and circumstances render application of the rule inequitable, unduly burdensome or otherwise contrary to the public interest, and there is no reasonable alternative.[18] CBT's petition for unconditional waiver of Section 24.204 fails to

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[15] *Id.*

[16] Ameritech Comments at 1-2.

[17] CBT Reply at 1-3. The proposals by Ameritech and others addressing post-auction divestiture of otherwise disqualifying cellular interests are considered in our *Broadband PCS Reconsideration Order*, *supra* n.4 at paras. 30-34.

[18] Section 24.819 of the Commission's Rules specifically incorporates this standard in the PCS context. *See Fifth Report and Order*, 59 FR 37566, 37613 (July 22, 1994); *see also* Northeast Cellular Telephone Co., L.P. v. FCC, 897 F.2d 1164, 1166 (D.C. Cir. 1990); WAIT Radio v. FCC, 418 F.2d 1153 (D.C. Cir. 1969).

satisfy either aspect of the waiver standard.

10. CBT's arguments that our cellular/PCS cross-ownership restrictions are too stringent, and should be limited to instances where demonstrable control over an in-market cellular license exists, are actually an attack on the substance of Section 24.204. These claims do not demonstrate that the rule as it applies to CBT's particular circumstances fails to promote the purposes for which it is designed. In fact, we specifically rejected identical arguments in the PCS Rulemaking proceeding.[19] We will not revisit that decision in the context of this waiver request.

11. Section 24.204 is designed to increase the number of unaffiliated competitors in each PCS market and to safeguard the competitiveness of those markets by excluding entities whose significant, in-market cellular holdings create incentives for them to act anticompetitively. CBT contends that application of the rule in its circumstances is unreasonable because a "financially punitive" partnership agreement and the Partnership's poor financial performance allegedly render CBT unable to divest its cellular interest at a price reasonably reflecting CBT's view of the value of that interest.[20] Even assuming, arguendo, that CBT's characterizations of the agreement and the Partnership's financial performance are accurate,[21] we are not persuaded that the financial consequences of withdrawal from a partnership voluntarily entered by CBT, whatever they may be, constitute sufficient grounds for the unconditional waiver requested by CBT.

12. Nonetheless, we are persuaded that CBT's circumstances are sufficiently unique to warrant a limited waiver of one part of Section 24.204. As noted previously, that rule permits entities with attributable, in-market cellular interests to participate in the auction of 30 MHz broadband PCS licenses on condition that they divest any prohibited cellular interest within 90 days following license grant.[22] It is unlikely that

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[19] *See, e.g.*, Memorandum Opinion and Order, FCC 94-144, June 13, 1994, at paras. 98-122, *summarized* 59 FR 32820 (June 24, 1994).

[20] CBT Addendum at 2-3.

[21] Ameritech denies CBT's allegations. *See* Ameritech Comments at 2.

[22] Third Memorandum Opinion and Order, Amendment of the Commission's Rules to Establish New Personal Communications Services, GEN Docket No. 90-314, FCC 94-265, Oct. 19, 1994, at

CBT's efforts to dissolve the Partnership through litigation in Delaware will be concluded in time to satisfy the post-auction divestiture deadline in Section 24.204. If CBT is successful in its litigation it expects to dissolve the Partnership and resolve the cross-ownership conflict. We note that this litigation was initiated prior to the first broadband PCS auction, and, according to CBT, for the purpose of divesting a cellular interest that conflicts with our cross-ownership restrictions. On this record we have no reason to believe that this litigation may continue substantially beyond the anticipated period for usual licensing procedures and related divestiture requirements.

13. We have previously granted a temporary waiver of our cross-ownership rules where the compliance delay associated with unresolved proceedings might work a hardship by precluding parties from actions they would be eligible to undertake when the proceedings are concluded.[23] Given the analogous difficulties potentially confronting CBT, we conclude that the public interest will be served by affording CBT additional flexibility, if needed, to comply with the post-auction divestiture requirement of Section 24.204(f). In the event CBT is a winning bidder in the forthcoming auction of in-market 30 MHz broadband PCS licenses, or otherwise acquires an attributable interest in such a license, and the 90 day time period for CBT to comply with the post-auction divestiture requirement expires with the litigation still unresolved, we will allow CBT an additional ninety days in which to divest the interest. Thus CBT (or an entity in which CBT has an attributable interest), if it is otherwise qualified to obtain a PCS license, will have 180 days from grant of a PCS license to CBT to come into compliance with Section 24.204. Should the litigation continue, CBT may seek further relief. We delegate to the relevant licensing Bureau the authority to address any such extension request, which should be evaluated based on the criteria set forth above and the policies developed in Docket 90-314. CBT is on notice that we are not inclined to permit it to hold impermissible attributable interests indefinitely.

14. Accordingly, IT IS THEREFORE ORDERED, that the petition for waiver of Section 24.204 of the Commission's Rules, 47 C.F.R. §24.204, filed by Cincinnati Bell Telephone, IS GRANTED to the extent described above and in all other respects IS DENIED.

15. IT IS FURTHER ORDERED that the relevant licensing Bureau shall impose the following condition on any broadband PCS

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paras. 33-34.

[23] *See* Request by Pacific Telesis Group and PacTel Corporation for a Waiver of Section 99.204 of the Commission's Rules, FCC 94-8, released Jan. 8, 1994.

license obtained by Cincinnati Bell Telephone or an entity in which Cincinnati Bell Telephone has an attributable interest, grant of which would result in a violation of Section 24.204 of the Commission's Rules: The licensee shall come into compliance with the limitations on common ownership of cellular and broadband PCS interests set forth in 47 C.F.R. § 24.204 within 180 days of final grant, and the licensee shall submit, within that time period, a certification that it and all parties to the license application have come into compliance with those limitations.

16. IT IS FURTHER ORDERED that we delegate to the relevant licensing Bureau the authority to address any request for further relief by Cincinnati Bell Telephone or an entity in which Cincinnati Bell Telephone has an attributable interest, which shall be evaluated based on the criteria set forth above and the policies developed in Docket 90-314.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

Before the
FEDERAL COMMUNICATIONS COMMISSION FCC 94-293
Washington, D.C. 20554

In the Matter of	)	
	)	
Amendment of Parts 21 and 74 of the	)	
Commission's Rules With Regard to	)	MM Docket No. 94-131
Filing Procedures in the Multipoint	)	
Distribution Service and in the	)	
Instructional Television Fixed Service	)	
	)	
and	)	
	)	
Implementation of Section 309(j) of the	)	PP Docket No. 93-253
Communications Act - Competitive Bidding	)	

NOTICE OF PROPOSED RULEMAKING

Adopted: November 10, 1994 Released: December 1, 1994

Comments Due: January 9, 1995
Reply Comments Due: January 24, 1995

By the Commission:

I. INTRODUCTION

1. By this action, the Commission proposes to streamline the procedures by which applications for new facilities in the Multipoint Distribution Service (MDS)[1] are filed and processed. We propose to adopt filing procedures consistent with our competitive bidding procedures. To do this, we propose that applicants file short-form applications for predetermined geographic areas and the successful bidders file long-form applications. We believe that implementation of this process would avoid the lengthy delay associated with licensing stations site-by-site, and therefore would allow operators to enhance their service more rapidly, providing more competition to wired cable. However, we also invite comment on alternative filing procedures, including a national filing window and one limited to existing licensees and system operators. We solicit comment on the technical and practical feasibility of utilizing a mandatory electronic filing approach in conjunction with each of

[1] In this proceeding, unless otherwise indicated, "MDS" includes single channel and multichannel applications and authorizations collectively.

these filing approaches.[2] Finally, we invite any other proposals that would allow the Commission to process MDS applications for new stations more efficiently and result in more MDS service opportunities becoming available to the public. We limit the scope of this proceeding to revisions to our rules and procedures that will improve the MDS application processes.[3]

2. Our goal in instituting this proceeding is to facilitate development of the wireless cable industry[4] and to continue our efforts to coordinate the processing of MDS and ITFS applications. The Commission has consistently maintained that, in providing communications services, the public interest is better served by competition. A competitive industry framework promotes lower prices for services, provides incentives for operators to improve those services and stimulates economic growth. An essential component of competition is choice. As we recognized in our recent report to Congress, consumers in the market for video programming do not have enough choices.[5] Although competing technologies have made major strides since the previous report on cable competition in 1990, the cable television market remains largely noncompetitive. With respect to wireless cable, we reported that more systems are being built, the number of subscribers has increased, and program access provisions and changes in other regulations have given wireless cable operators a better foothold in competition with wired cable, including the credibility to gain access to financing. *Competition Report* at paras. 79, 80 and 90. However, the difficulty of

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[2] There is now outstanding an *Order and Further Notice of Proposed Rulemaking* in MM Docket No. 93-24, 9 FCC Rcd 3348 (1994), in which the Commission is considering further improvements to the Instructional Television Fixed Service (ITFS) licensing process, including adoption of a window filing procedure. The only aspect of this proceeding which we propose to apply to ITFS is the electronic filing proposal.

[3] As noted in footnote 2, *supra*, the electronic filing proposal if implemented would also apply to the ITFS application proceeding. In response to a July 28, 1993 *Public Notice*, we received several comments on ways the Commission could expedite the processing of MDS applications. We have considered those views in our drafting of this *Notice of Proposed Rulemaking* and we will incorporate those materials in the public record of this proceeding.

[4] "Wireless cable" is the delivery of video programming to subscribers using MDS and/or ITFS channels. Wireless cable resembles cable television, but instead of coaxial cable, wireless cable uses microwave channels. Our use of the term "wireless cable" does not imply that it constitutes cable television for statutory or regulatory purposes.

[5] *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming* (*Competition Report*), CS Docket No. 94-48, FCC 94-235 (released Sept. 28, 1994). The Commission is required to file such annual reports pursuant to the Cable Television Consumer Protection and Competition Act of 1992 (1992 Cable Act), Pub. L. No. 102-385, Section 628(g), 106 Stat. 1460 (amending the Communications Act of 1934), codified at 47 U.S.C. Section 548(g).

accumulating sufficient channel capacity remains a major obstacle to many wireless cable operators. According to the *Competition Report*, the combination of administrative improvements in wireless cable licensing and the use of digital compression[6] should help to alleviate this problem in the future. *Id.* at para. 90. This rulemaking is one of several administrative improvements directed toward enhancing the development of wireless cable operators as viable competitors in the video programming marketplace. It will also further the policies set forth by Congress in the 1992 Cable Act to ". . . promote the availability to the public of a diversity of views and information through cable television and other video distribution media."[7]

II. BACKGROUND

3. When the Commission reallocated eight channels to MDS in 1983, thereby creating wireless cable as a multichannel video distribution medium, a variety of application procedures existed because wireless cable system operators used a combination of channels accumulated from a variety of Commission services with differing sets of rules, procedures and policies.[8] One of the major obstacles faced by wireless cable operators over the years has been the difficulty involved in accumulating the number of channels necessary to meet subscriber demand and be able to compete with wired cable television systems in the same

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[6] Digital compression is a technology that employs various techniques to reduce the number of bits required to transmit a program. Therefore, for a given channel bandwidth and digital transmission rate, an operator may, depending on circumstances, transmit a single uncompressed program or multiple compressed programs. For example, a six-to-one compression ratio permits the operator to offer six program channels from one 6 MHz frequency bandwidth.

[7] 1992 Cable Act Section 2(b)(1), 106 Stat. at 1463. An essential element of the 1992 Cable Act is promoting increased competition and diversity by fostering the development of alternative multichannel video programming distributors (MVPD). The term "MVPD" means "a person such as, but not limited to, a cable operator, a multichannel multipoint distribution service, a direct broadcast satellite service, or a television receive-only satellite program distributor, who makes available for purchase, by subscribers or customers, multiple channels of video programming." Communications Act Section 602(12), 47 U.S.C. Section 522(12). In markets where effective competition is present, the government will no longer need to regulate cable rates, as required by the 1992 Cable Act, because cable rates will be regulated by the marketplace. Communications Act Section 623(a)(2), 47 U.S.C. Section 543(a)(2).

[8] *Report and Order* in Gen. Docket No. 80-112, 94 FCC 2d 1203 (1983). Therein, the Commission reallocated eight of the ITFS channels for use by MDS nationally, grandfathered interference protection to existing E or F ITFS applicants, permittees or licensees, approved cash payments by MDS entities for vacating ITFS channels, and authorized ITFS licensees to lease the excess capacity on their systems to wireless cable operators.

area. There are a maximum of thirty-three microwave channels available for wireless cable systems. This includes thirteen MDS channels (Channels 1, 2 or 2A, E1-E4, F1-F4 and H1-H3) and the excess capacity in the twenty ITFS channels (Channels A1-A4, B1-B4, C1-C4, D1-D4 and G1-G4).[9] In an effort to consolidate and promote the expeditious processing of applications for licenses that may be used to provide wireless cable services into one organization, the Commission recently transferred responsibility for MDS from the Common Carrier Bureau to the Mass Media Bureau. *Amendment of Parts 0 and 1 of the Commission's Rules to Reflect a Reorganization of Multipoint and Multichannel Multipoint Distribution Services*, 9 FCC Rcd 3661 (1994).

4. For a number of years, the Commission has been concerned that the volume of MDS applications filed by speculators has caused delays in the licensing process and has overburdened the Commission's limited resources. A rule revision aimed at addressing this problem was adopted in the *Report and Order* in Gen. Docket Nos. 90-54, 80-113, 5 FCC Rcd 6410, 6424 (1990); *Order on Reconsideration*, Gen. Docket Nos. 90-54, 80-113, 6 FCC Rcd 6764 (1991), *petition for review filed, United States Independent Microwave Television Association v. FCC and United States of America*, No. 91-1637 (D.C. Cir. filed Dec. 20, 1991) (held in abeyance by Court Order of February 21, 1992, pending action on the second set of reconsideration petitions). The rule, commonly referred to as the "same calendar day rule" is found in Section 21.914 of the Commission's rules, 47 C.F.R. Section 21.914. Under this rule, an MDS application for a new station that is acceptable for filing will be mutually exclusive with any other MDS application which is acceptable for filing for the same service area and frequency if it is received by the Commission on the same calendar day as the first such MDS application received by the Commission. This rule change eliminated the opportunity for speculators simply to copy applications that were previously filed and resubmit them under different names. However, because of our rules authorizing lotteries and settlement groups, the filing of applications for new MDS stations was nevertheless appealing to speculators, who continued to file a large number of applications up to the time the Commission imposed a freeze on the filing of applications for new facilities in

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[9] In some locales, there are twenty-eight ITFS channels due to the 1983 grandfathering of ITFS entities. In 1991, the Commission reallocated the H-group channels from the Operational Fixed Service to MDS and made MDS operators eligible for authorization on vacant ITFS channels with specified restrictions. *Second Report and Order* in Gen. Docket No. 90-54, 6 FCC Rcd 6792, 6793-94, 6801-06 (1991). In 1992, the frequency spectrum of 2160 MHz to 2162 MHz (of the former frequency allocation of 2156 MHz to 2162 MHz, MDS Channel 2) was reallocated to emerging technologies, leaving MDS Channel 2A, a 4 MHz channel. *Redevelopment of Spectrum to Encourage Innovation in the Use of New Telecommunications Technologies*, ET Docket No. 92-9, 7 FCC Rcd 6886, 6889 n.22 (1992).

the *Notice of Proposed Rulemaking*, PR Docket No. 92-80, 7 FCC Rcd 3266 (1992).[10] At the time of the freeze, there was a backlog of tens of thousands of applications, the majority believed to be speculative. *Id.* at 3267.

5. The Commission has recently stated that all mutually exclusive MDS applications for new stations filed after the lifting of the freeze will be subject to the competitive bidding process. *Implementation of Section 309(j) of the Communications Act - Competitive Bidding, Second Report and Order* in PP Docket No. 93-253, 9 FCC Rcd 2348, 2359 (1994) (*Second Report and Order*), *recon. granted in part, Second Memorandum Opinion and Order*, FCC No. 94-215 (released Aug. 15, 1994), 59 Fed. Reg. 44,272 (Aug. 26, 1994). Therein, the Commission determined that the use of competitive bidding for MDS would further the objectives described in 47 U.S.C. Section 309(j)(3). The use of competitive bidding would speed the development and further deployment of MDS for the benefit of the public, with minimal administrative or judicial delays. The proposals set forth for consideration in this proceeding are designed to avoid the backlogged applications and legal protests that have delayed and stifled the deployment of MDS in the past. We believe that accelerated processing permitted by electronic filing and data collection, along with competitive bidding procedures, will reduce the likelihood of speculative filings and generally expedite the initiation of new service.

III. DISCUSSION

6. In the discussion that follows, we invite comment on several alternatives for acceptance of MDS applications after the processing freeze is lifted next year. The Commission favors a filing approach which is based upon specific predetermined geographic areas, such as Metropolitan Statistical Areas (MSA) and Rural Service Areas (RSA) or Areas of Dominant Influence (ADI). This filing approach would utilize short-form applications to identify mutually exclusive applicants for competitive bidding purposes. *Second Report and Order* in PP Docket No. 93-253, 9 FCC Rcd 2348, 2376 (1994). Another filing approach would restrict applications to Commission-identified vacant E, F and H channels. Here, the Commission would also identify mutually exclusive situations through the use of short-form applications. Under another alternative, the Commission would periodically open national filing windows, and there would be no geographic restrictions on filing for available MDS channels. One option to the national filing window approach would be to limit eligibility to file in the first window to existing system operators and licensees. These two national window proposals would require long-form applications, containing the applicant's complete technical proposal, to determine mutual exclusivity before competitive bidding procedures are implemented.

7. ***MSA/RSA/ADI Approach.*** As our preferred filing approach, we invite comment

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[10] The Commission adopted a number of rule changes to deter systematic abuse by speculators in *Report and Order* in PR Docket No. 92-80, 8 FCC Rcd 1444 (1993).

on whether we should adopt a procedure under which applications for new MDS stations would be filed for predetermined, discrete areas, similar to Cellular Radio's Metropolitan Statistical Areas (MSA) and Rural Service Areas (RSA), or the television Areas of Dominant Influence (ADI).[11] The Commission would release a public notice announcing auctions by MSA/RSA/ADI, and the time, place and method of competitive bidding to be used, including the applicable bidding procedures. Applicants would file for all usable E, F and H channels. They would be allowed to operate facilities on these channels anywhere throughout the service area provided the specific engineering design of their wireless cable facility meets the Commission's interference protection standards to any previously proposed or authorized MDS facilities. The public notice would also specify the filing period for short-form applications (FCC Form 175)[12] and deadlines for submitting the applicable filing fee and the upfront payment, and the amounts. Applicants would file a short-form application for all usable channels in a particular MSA, RSA or ADI and those applications would be treated as mutually exclusive and subject to the competitive bidding process. Mutually exclusive applicants would bid for all usable channels in a particular area as a package, enabling operators to amass large channel groups.

8. We seek comment on whether our current 15 mile radius definition of an MDS licensee's protected service area would be appropriate for licenses granted on an MSA/RSA/ADI basis. In particular, we request comment on whether the MSA/RSA/ADI boundary should become the protected service area of the wireless cable system. If this definition of protected service area were adopted, how would our current interference protection standards, defined by desired-to-undesired signal strength ratios, be applied? Would these standards permit service to the areas adjacent to the borders between geographic license areas? If not, are there modifications to the rules that might serve the public interest, for example, permitting parties to negotiate interference rights to enable interference-free service in the border areas? We also request comment on the impact of our protected service

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[11] MSAs and RSAs are standard geographic areas used by the Commission for administrative convenience in the licensing of cellular radio systems. All of the 306 MSAs and 428 RSAs and the counties they comprise are listed in *Public Notice* Report No. CL-92-40 "Common Carrier Public Mobile Services Information, Cellular MSA/RSA Markets and Counties," DA 92-109, 7 FCC Rcd 742 (1992). *See also* 47 C.F.R. Section 22.909 (effective Jan. 1, 1995). ADIs are standard geographic areas developed by Arbitron Ratings Company. Under this market definition, each county in the continental United States is placed within one of 210 ADIs, the lowest numbered ADI having the highest population.

[12] Form 175 contains the applicant's name, the licenses on which the applicant wishes to bid, the persons authorized to make or withdraw a bid, whether the applicant is qualified as a designated entity under 47 C.F.R. Section 1.2110, certifications that the applicant is legally, technically, financially and otherwise qualified, and identification of all parties involved in agreements, or certification that no agreements exist, relating to the conditional licenses being auctioned or the bidding process.

area decision on the ordering in which service areas should be auctioned. For example, depending on the definition of protected service areas, service areas auctioned earlier may be able to secure border area interference protection rights. In this case, should service areas be auctioned in descending order of population?

9. The auction winner would have several responsibilities and rights. For instance, an auction winner would be required to submit a down payment within five business days after the close of the auction. The auction winner would be required, by a specified date, to file a long-form MDS application which includes a complete engineering proposal. This long-form would include a demonstration that the proposed MDS stations would not cause harmful interference to any previously proposed or authorized MDS stations, and applicants would have the opportunity to cure any such defects in their engineering. Long-form applications found to be acceptable would be proposed for grant by a Commission public notice. This public notice would trigger a thirty-day period for the filing of petitions to deny. *See* 47 U.S.C. Section 309(b). If there are no petitions filed, or upon resolution of petitions that have been filed, and if the applicant is otherwise qualified under 47 C.F.R. Section 21.32 (*e.g.*, FAA clearance), the conditional license would be granted. If the conditional license was granted following an auction, the grant would be conditioned upon the winner making full payment of the balance of the winning bid within five business days following the grant (except for small businesses allowed to make installment payments).[13] Since applicants would receive conditional licenses for all usable channels in a particular area as a package, we seek comment as to the appropriateness of allowing mergers and other transfers prior to the completion of construction.

10. The Commission believes that this framework provides the most manageable and efficient system to disseminate MDS licenses. The use of short-form applications prior to the auction reduces the administrative burdens on applicants and the Commission, and minimizes the potential for delay. In addition, this type of filing approach, coupled with competitive bidding procedures, would encourage universal coverage and afford the greatest likelihood of rapidly promoting the development of MDS as a viable competitive service. This approach is also likely to deter speculation because auction methodologies are designed to ensure that the party who most highly values the spectrum obtains the license, not a speculator. We solicit comment on whether we should adopt this proposal, and if so, which geographic areas are most suitable for MDS to utilize.

11. ***E, F and H Identified Sites.*** An alternative filing approach, which is somewhat more restrictive than our preferred approach, would limit applications to predetermined sites. We invite comment on a procedure pursuant to which multiple public notices would identify sites where there are vacant E, F or H channels available. The Commission would identify such sites based upon the location of an already authorized E, F or H channel. Pursuant to this proposal, applicants for the vacant channels at these identified sites would file a short-

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[13] The definition of "small business" is discussed in paragraph 24, *infra*.

form application to identify mutually exclusive situations for purposes of competitive bidding. Thereafter, the auction winner would be required to file a long-form MDS application which contains a complete engineering proposal, specifying compatible station design and demonstrating a lack of harmful interference to co-channel and adjacent-channel previously proposed or authorized MDS stations in nearby areas. We request comment on this alternative, which also promotes streamlined application processing and works well with competitive bidding procedures.

12. ***National Filing Window Proposal.*** Under this proposal, windows would be opened periodically in order to provide opportunities for filing applications for new MDS stations.[14] The Commission would issue a public notice announcing the filing window for available channels which would remain open for a specified period of time, and applications for new MDS stations would be filed within that stated window. Under this approach, there would be no geographic restrictions upon filing for available MDS channels. Accordingly, the applicant would initially be required to file a long-form MDS application, with the applicant's complete engineering proposal, to enable the Commission to determine mutual exclusivity. After the close of the window, each application would undergo an acceptability review, which includes an engineering interference analysis. To be acceptable for filing, the application would have to contain all of the data and other information necessary to allow processing of the application. *See* Appendix A, Items 1-20. An application would be considered unacceptable for filing and returned if, *inter alia*, its proposed facilities are predicted to cause harmful interference to any part of the protected service area of an authorized station or a facility proposed in an application filed prior to the opening of a particular filing window. *See* 47 C.F.R. Sections 21.31, 21.902 and 21.914. Applications found to be acceptable and not mutually exclusive with any other acceptable application would be proposed for grant by a Commission public notice. This public notice would trigger a thirty-day period for the filing of petitions to deny. *See* 47 U.S.C. Section 309(b). If there are no petitions filed and if the applicant is otherwise qualified, the conditional license would be granted. Applications found acceptable for filing and mutually exclusive with another would be subject to competitive bidding. Under the national window approach, applications may be amended while the window is open. After the close of the window and up until the close of the auction, no amendment may be filed which corrects any defect in an application that is unacceptable for filing on the last day of a filing window. We propose that the Commission only accept the following two types of amendments after the close of the window and up until the close of the auction: (1) amendments filed pursuant to 47 C.F.R. Section 1.65 to furnish updated information, and (2) minor amendments as defined by 47 C.F.R. Section 21.23, including *pro forma* changes in ownership or control. Following the auction, the Commission would provide the auction winner the opportunity to cure any defects in its engineering proposal.

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[14] A similar procedure is currently being used by the low power television service. *Report and Order* in MM Docket No. 83-1350, 102 FCC 2d 295 (1984).

13. We believe that since this approach would likely result in a larger number of mutually exclusive applications, implementation would require significant resources and take a substantial amount of time to conduct the competitive bidding process. We request comment on how to resolve the "daisy-chains" (interlinking application proposals at different locations) that might arise under this proposal. We invite commenters favoring a national window approach to discuss these concerns, how far in advance we should announce the opening of a window and the appropriate length of the window.

14. ***First Window: Accumulation of "Critical Mass" of Channels.*** As an option to the national filing window, the first window could be limited to existing system operators and licensees. Under this approach, we would require that applications be filed by a licensee or system operator who, at the time the application is filed, is operating a minimum number of channels, such as four, six, eight or ten. Where the existing system operator is not a licensee, we would require a certification that lease agreements have been executed between the operator and the licensee. We would require such applicants to keep copies of lease agreements and make them available upon the request of the Commission. This "critical mass" approach would encourage enhancement of existing wireless cable operations, and thus accelerate opportunities for competition with wired cable systems in various locales. Such an approach is well within our legal authority. *See, e.g., United States v. Storer Broadcasting Co.*, 351 U.S. 192, 202 (1956); *Ashbacker Radio Corp. v. FCC*, 326 U.S. 327, 333 n.9 (1945); *Hispanic Information & Telecommunications Network v. FCC*, 865 F.2d 1289, 1294 (D.C. Cir. 1989). We solicit comment on whether we should adopt this proposal, and if so, who should be eligible to file applications in this window.

15. ***Interference Criteria and Mutual Exclusivity.*** As a complement to the various filing proposals and electronic procedures, *infra*, we propose to adopt a technical equation as the basis for the "free space" interference protection calculations. The following formula is currently used by the Commission's MDS engineers and is recognized by engineering consulting firms that represent the wireless cable industry:

> The received signal power level $(RSL)_{dBW}$ at the output of the FCC reference receiving antenna is obtained from the following: [15]
>
> $$(RSL)_{dBW} = (EIRP)_{dBW} - (L_{FS})_{dB} + (G_{AR})_{dB}$$
>
> where the free space loss $(L_{FS})_{dB}$ is
>
> $$(L_{FS})_{dB} = 20 \log (4\pi rd/\lambda) \text{ dB}$$

In these equations, $(RSL)_{dBW}$ is received power in decibels referenced to one watt, $(EIRP)_{dBW}$

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[15] Leon W. Couch II, Digital and Analog Communication Systems, p. 384 (3rd ed. 1990).

is equivalent isotropically radiated power in decibels above one watt, d is the distance of the signal path in meters, λ is the wavelength of the signal in meters, and G_{AR} is the gain of the reference receiving antenna, as obtained in 47 C.F.R. Section 21.902(f)(3), Figure 1. We propose to formalize the above equations by adopting them as a rule provision, much like the equation at 47 C.F.R. Section 21.902(d)(2). In so doing, we are not proposing significant changes in the substantive requirements regarding interference showings. To facilitate our plans for computerized interference studies, we will require proposed facilities to meet the 45 dB and 0 dB co-channel and adjacent-channel desired to undesired signal strength ratios at points along the service contours of protected facilities which were authorized under the current interference standards. With regard to long-form applications, we propose to retain the rules requiring that the applicant perform analyses of the potential for harmful interference and serve the interference studies upon the previously proposed or authorized station applicants, conditional licensees or licensees required to be studied. 47 C.F.R. Section 21.902. On the electronic application form, the applicant would supply certain crucial data elements describing the station parameters, such as antenna polarization and the station equivalent isotropically radiated power (EIRP), while the Commission staff would perform the interference analysis using a computer program. In this service, there are two rules that currently define mutual exclusivity: Section 21.31 and Section 21.901(d)(5). *See* 47 C.F.R. Section 21.902. In light of the proposed computer-assisted interference studies that will readily determine whether an application is mutually exclusive with another, under our national window proposals, the second rule, Section 21.901(d)(5), is no longer necessary. We would not require the submission of any types of interference or other engineering analyses to the Commission at the time the application is filed. Nor would we require the submission of a list of each applicant, conditional licensee or licensee served at the time the application is filed. We propose to require the applicant to make the records available for Commission inspection upon request. We invite comment on whether we should adopt this formula as a rule. We also seek comment on whether we should eliminate signal contour maps as a required part of interference studies.

16. We are also proposing to improve the current application form used for new MDS stations, FCC Form 494,[16] by excluding certain data elements which have yielded information that is no longer necessary or of only marginal utility. Further, such modifications should serve to facilitate the proposed computer-assisted process. For instance, we propose to eliminate queries regarding the antenna vertical sketch and the narrative description of why grant of the application would be in the public interest. We also generally propose to exclude the following parameters of the transmission system: transmitter manufacturer and model number, transmitter output power, transmitting antenna gain and the specification of transmission line and other transmission losses. With regard to transmitters, we are only concerned that MDS licensees operate transmitters that are "type-accepted" by the Commission for use in this service. Although we propose to eliminate the requirement

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[16] Since Form 494 is a multi-purpose form that is used for other services, to the extent that we are proposing changes, we intend to create a different form to be used for MDS.

that the applicant identify the transmitter make and model, we intend to require conditional licensees to certify the use of a type-accepted transmitter in their certification of construction, currently FCC Form 494A. Transmitter output power, system loss, and antenna gain are the parameters used to calculate a station's maximum EIRP. The MDS rules were recently changed to provide for a maximum EIRP, rather than a maximum value for transmitter output power. *See* 47 C.F.R. Section 21.904. The critical parameter in free space signal propagation analysis is EIRP. Applicants, therefore, would be permitted to use any transmitter output power necessary to achieve the desired EIRP, provided the EIRP remained within the limits given in the Commission's rules. Thus, we believe that it is not necessary to require applicants to specify the equipment parameters used to calculate the EIRP, *i.e.*, transmitter power, antenna gain and transmission losses. We also propose to allow changes to these transmission parameters without notification to the Commission, provided the resulting EIRP would not change. The station power to be specified on the form would be the maximum EIRP in the horizontal plane, *i.e.*, the EIRP at an angle of zero degrees in the vertical plane. Electrical beam tilting of antennas will be permitted; however, in all cases, applicants would be required to specify the EIRP in the horizontal plane. In most instances, this value of EIRP closely approximates the power radiated to the radio horizon which is most relevant to interference analysis. Also, by proceeding in this manner, it would not be necessary for us to collect data on antenna vertical radiation patterns. We invite commenters to discuss these and other possible changes to an application form for MDS facilities and the related issues introduced in this proceeding.

17. ***An Electronic Application Form.*** We propose to modify further the long-form MDS application in an effort to make the form compatible with an electronic filing system. The proposed electronic version of the long-form application for new MDS stations would consolidate information from FCC Form 494 and FCC Form 430, the License Qualification Report, and be formatted in a manner appropriate for electronic data capture. For example, we would retain engineering data elements necessary for analysis of interference or possible air safety hazards, and we would retain applicant responses which demonstrate compliance with a particular statutory requirement, such as an environmental assessment. In terms of specific items, Appendix A lists proposed data elements and other informational items for our new electronic application form. These include general, engineering and legal elements. The engineering parameters of proposed stations are generally limited to variables used in our interference analysis or air safety determinations, such as transmitting antenna site coordinates, EIRP, antenna polarization, site elevation and antenna structure height above ground. Other data may be used to verify an applicant's compliance with a particular Commission rule. For example, antenna beam width is used to calculate the maximum allowable EIRP of a station using a directional transmitting antenna. Applicants proposing to locate stations in areas where notification or coordination with Canada or Mexico is required by international agreement would be required to submit the following additional technical data, which is not proposed as standard data elements in the electronic application form: transmitter output power, transmitting antenna gain and transmission line loss. It may be possible to specify this data in a textual exhibit in the electronic long-form application. If not, a paper supplement to the application would be submitted as directed by the

Commission staff. We seek comment on our proposed elements for the electronic filing process.

18. *Electronic Filing Process*. In 1992, Congress amended the Communications Act of 1934 to permit the electronic filing of license and construction permit applications. Telecommunications Authorization Act of 1992, Pub. L. No. 102-538, Section 204, 106 Stat. 3533, 3543, codified at 47 U.S.C. Sections 308(b) and 319(a). Such applications may be signed "in any manner or form, including by electronic means, as the Commission may prescribe by regulation." *Id*. The Commission currently accepts license applications electronically in the private land mobile radio service (FCC Form 574) and we are here considering a proposal to accept electronically applications for new MDS stations.[17] We would modify our handwritten signature requirement, 47 C.F.R. Sections 1.743 and 21.6(d), and other rules as necessary to implement such an electronic filing system.

19. We envision the use of communication links, such as a Value Added Network (VAN), that would allow the exchange of data between applicants and the Commission. VANs are offered by private entities and may require an applicant to establish an account. The use of a VAN is particularly attractive as a method of electronically filing applications because of its high degree of efficiency and security in transferring information. Although our intent is to implement an electronic filing system without creating additional burdens, we recognize that VANs may impose an added cost to filing an application. For example, to establish an electronic mailbox from a VAN may cost as much as $300 with added monthly and per use fees. To minimize the costs to individuals, an electronic mailbox could be established by a representative group, such as a law firm or engineering consulting firm, as a service to its customers.

20. In designing an electronic filing system that will work efficiently, we believe that it will be necessary to eliminate the filing of paper to the maximum extent possible. Such a system would consist of data on a series of computer screens, translated into a transaction format, together with electronically prepared exhibits. We envision an electronic form designed for personal computers using a windows-based environment. Essentially, the data would be uploaded from a personal computer to a VAN or other type of electronic mailbox, then downloaded to a Commission mailbox in the correct format. Although it appears that VANs may have the capability to transfer text electronically, a possible limitation concerns

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[17] *Amendment of the Commission's Rules to Modify Signature Requirement for License Applications in the Private Radio Services*, 8 FCC Rcd 2662 (1993). Until we have gained some experience with electronic filing procedures, we propose to limit its use to the filing of applications and related amendments for new MDS stations. Certifications of completion of construction, applications for assignment or transfer of control of licenses, license renewals, signal boosters, extensions and modifications pursuant to 47 C.F.R. Sections 21.40, 21.41, 21.42 and 21.910, would continue to be filed in paper format according to existing procedures.

the difficulty or expense associated with electronic maps or other graphic representations. For routine applications, we hope to eliminate the need for paper submissions completely, at least during the initial application acceptance stage of processing. Implementing such a system would expedite the application process in several ways. First and foremost, it would eliminate the need for manual entry of application data into the Commission's several databases, resulting in instant databases that are current and accurate. Our intent is for the public to have on-line viewing access to MDS databases through a third-party vendor and the Commission's public reference room. Second, an electronic filing system, coupled with the proposed computer-assisted processing program, would eliminate the need for manual review by the Commission's engineering staff of engineering analyses currently submitted by applicants under 47 C.F.R. Sections 21.902 and 21.904. This manual review is very time-consuming. Finally, the staff would be able to handle, with reasonable speed, the anticipated increase in the number of applications to be processed. In balancing these multiple factors, we believe that the benefits of implementing an electronic filing system outweigh the associated costs. We invite comment on the feasibility of using a mandatory electronic filing system for new MDS station applications in connection with the application filing procedures discussed above. We also solicit comment on whether ITFS applicants should be required to file applications for new stations electronically on a combined application form, and whether there should be a paper exception for those educators that are not financially supported by a wireless cable operator.

21. ***Electronic Fee Payments***. Regarding payments of application fees, we will use the current methods of payment for application fees under 47 C.F.R. Section 1.1109. The methods include check, bank draft, money order, wire transfer, electronic customer-initiated payments and Visa or Master Card credit card. The Commission recently amended 47 C.F.R. Sections 1.1108 and 1.1109 to permit the electronic filing of fee payments, initially on an experimental basis. *Implementation of Section 9 of the Communications Act, Report and Order* in MD Docket No. 94-19, FCC No. 94-140 (released June 8, 1994), 59 Fed. Reg. 30,984 (June 16, 1994) at para. 50-51. In addition to the existing payment methods available, we propose to accept electronic payments under Section 1.1109. Pursuant to subsection (a)(1) of that section, procedures for the electronic payment of fees will be announced by Public Notice. We request comment on a fee system where applicants use a unique fee payor number, such as a federal employer identification number together with an appropriate service code, and a suffix in cases where applicants file multiple applications. This would link the fee payment with the electronically filed application. Applicants would be permitted to prepay their application fee after public notice of any national filing window until the close of the filing window, using any currently acceptable form of payment. When the applicant makes the fee payment to the Commission's lockbox bank, the applicant's unique identification number is supplied with the fee payment, and the applicant uses the same number on the electronic application for a new station. We seek comment on this proposal.

22. ***Competitive Bidding Procedures.*** In light of the proposals set forth above, we invite further comment on the *Notice of Proposed Rulemaking* in PP Docket No. 93-253, 8

FCC Rcd 7635 (1993) and the *Second Report and Order*, 9 FCC Rcd 2348, 2359 (1994), *recon. granted in part*, *Second Memorandum Opinion and Order*, FCC No. 94-215 (released Aug. 15, 1994), 59 Fed. Reg. 44,272 (Aug. 26, 1994), regarding competitive bidding procedures with respect to MDS. Specifically, we invite comment on which of the alternative competitive bidding procedures adopted in the *Second Report and Order* is best suited to MDS.

23. The *Second Report and Order* in the competitive bidding proceeding sets forth three primary auction methods from which the Commission may choose in selecting an appropriate competitive bidding design: (1) simultaneous multiple round auctions; (2) sequential oral auctions (open outcry); or (3) sealed bid auctions (either sequential or simultaneous). 9 FCC Rcd at 2366-67. We seek comment on the suitability of these methods for the auctioning of MDS licenses. There appears to be some geographic interdependence due to coordination of interference at the borders.[18] However, as the value of and interdependence between MDS licenses in different geographic areas may not be sufficiently high to justify the use of simultaneous multiple round bidding, we tentatively conclude that this type of bidding design is less appropriate for MDS than either sequential oral or sealed bid auctions. In commenting on this tentative conclusion, commenters should consider the relative value of MDS licenses, the importance for wireless cable operators of aggregating as many channels as possible within particular geographic areas, and the significance for operators of accumulating channels across diverse geographic areas. We additionally request comment on the relative advantages and disadvantages of utilizing either oral bidding or sealed bidding to auction MDS licenses. In commenting on the suitability of oral or sealed bidding for MDS, commenters should focus their discussion on the following factors: (a) the value and interdependence of MDS licenses; (b) the number of MDS channels that remain available for auction; (c) the expense to the Commission and to bidders; (d) the administrative ease of implementing the auction design selected; and (e) the expected number of bidders for each area. As explained in paragraph 7, *supra*, our preferred approach will utilize predetermined geographic service areas and contemplates auctioning all usable channels in each area together. We seek comment on this approach.

24. Section 309(j) of the Communications Act, which gave the Commission express authority to employ competitive bidding, also mandated that the Commission "ensure that small businesses, rural telephone companies, and businesses owned by members of minority groups and women are given the opportunity to participate in the provision of spectrum-based services." 47 U.S.C. Section 309(j)(4)(D). To implement this statutory mandate, the Commission established a menu of preferences, including installment payments, tax certificates, bidding credits and spectrum set-asides, to choose from in selecting preferences that will be applicable to particular services. *Second Report and Order* at 2389-92. We request comment on these various preferences, which entities should be eligible to receive

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[18] Licenses are interdependent when the value of a license to the bidder depends on the degree to which licenses are substitutes or complements. *Second Report and Order* at 2364.

them, and their appropriateness in light of the characteristics of MDS. In particular, with regard to determining eligibility for installment payments, we invite comment on the appropriate definition of "small business" to be employed, taking into account the capital requirements for MDS. Commenters may want to address whether the standard definition of "small business" utilized by the Small Business Administration is appropriate for MDS,[19] or whether we should establish a different standard based on a business' gross revenues.[20] We additionally seek comment on whether spectrum set-asides are appropriate for MDS. We also request comment on how to implement a bidding credit or payment discount program for MDS. In connection with preferences for designated entities, commenters may also wish to address measures designed to prevent unjust enrichment by trafficking licenses acquired through the use of preferences.

25. In addition to commenting on auction methods and preferences, commenters should address other issues related to competitive bidding for MDS. Commenters may want to comment on payment issues, particularly the appropriate amount of the upfront payment submitted prior to an auction, and the amount of the default penalty on winning bidders who fail to make their required down payments on licenses, fail to make final payments for licenses, or are disqualified after the close of an auction. Commenters may also wish to address the advisability of setting a reservation price, below which a license subject to auction will not be awarded. Provisions designed to prohibit collusive conduct in the context of competitive bidding may additionally be addressed, as should any other issues related to competitive bidding for MDS.

IV. PROCEDURAL MATTERS

26. As required by Section 603 of the Regulatory Flexibility Act of 1980, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. Section 601, *et seq.*, the Commission has prepared an Initial Regulatory Flexibility Analysis of the expected impact on small entities of the proposals suggested in this document. *See* Appendix B. We request written public comment

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[19] The Small Business Administration standard definition permits an applicant to qualify for financial assistance based on a net worth not in excess of six million dollars with average net income after federal income taxes for the two preceding years not in excess of two million dollars. 13 C.F.R. Section 121.802.

[20] For the broadband and narrowband Personal Communications Services, small businesses are defined as those with average gross revenues for the three preceding years of less than $40 million. It may be that this $40 million gross revenue standard is too high for MDS, given the more modest capital requirements of MDS operators. *Third Memorandum Opinion and Order and Further Notice of Proposed Rulemaking* in PP Docket No. 93-253, FCC No. 94-219 (released Aug. 17, 1994), 59 Fed. Reg. 44,058 (Aug. 26, 1994) at para. 46; *Fifth Report and Order* in PP Docket No. 93-253, FCC No. 94-178 (released July 15, 1994), 59 Fed. Reg. 37,566 (July 22, 1994) at para. 13.

on the analysis. Such comments must be filed in accordance with the same filing deadlines as comments filed in this rulemaking proceeding, but they must have a separate and distinct heading designating them as responses to the Initial Regulatory Flexibility Analysis. The Secretary shall send a copy of the *Notice of Proposed Rulemaking*, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with Section 603(a) of the Regulatory Flexibility Act.

27. For purposes of this nonrestricted notice and comment rulemaking proceeding, members of the public are advised that *ex parte* presentations are permitted, except during the Sunshine Agenda period, provided they are disclosed under the Commission's rules. *See generally*, 47 C.F.R. Sections 1.1202, 1.1203 and 1.1206(a).

28. The collection of information contained in this *Notice of Proposed Rulemaking* will be submitted to the Office of Management and Budget for review under Section 3504(h) of the Paperwork Reduction Act. 44 U.S.C. Section 3504(h). Copies of this submission may be purchased from the Commission's copy contractor, International Transcription Service, Inc., 2100 M Street, N.W., Suite 140, Washington, D.C. 20037, (202) 857-3800. Persons wishing to comment on this collection of information should file their comments with the Federal Communications Commission, Office of Managing Director, Paperwork Reduction Project, Washington, D.C. 20554, and the Office of Management and Budget, Paperwork Reduction Project, Washington, D.C. 20503. This *Notice* proposes further revisions to an existing collection of information, OMB No. 3060-0402, titled "Application for New or Modified Microwave Radio Station License Under Part 21" to create a separate paper application form to be used for new MDS facilities, and an electronic form to be used for new MDS and ITFS facilities. For further information regarding this collection of information, contact William Cline at (202) 418-0210, Records Management Branch, Office of Managing Director.

29. Pursuant to applicable procedures set forth in 47 C.F.R. Sections 1.415 and 1.419, interested parties may file comments on or before January 9, 1995, and reply comments on or before January 24, 1995. To file formally in this proceeding, you must file an original and five copies of all comments, reply comments, and supporting comments. If you want each Commissioner to receive a personal copy of your comments, you must file an original plus nine copies. You should send comments and reply comments to the Office of the Secretary, Federal Communications Commission, Washington, D.C. 20554. Comments and reply comments will be available for public inspection during regular business hours in the FCC Reference Center, Room 239, at the Federal Communications Commission, 1919 M Street, N.W., Washington, D.C. 20554.

30. For further information on this proceeding, please contact Sharon Bertelsen at (202) 416-0892 or Jerianne Timmerman at (202) 416-0881, Video Services Division, Mass Media Bureau.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

APPENDIX A

Proposed Long-Form MDS Data Elements for Electronic Filing

1. Applicant Name
   Mailing Address
   City, State and Zip Code
   (Area Code) and Telephone Number

2. Fee Payor Identification Number
   Payment Type Code
   Amount Paid

3. Service Area

4. Channel(s) Requested
   Frequency Offset, if Applicable

5. Proposed Transmitting Antenna Location
   City, County, State
   Address of Location
   Latitude and Longitude

6. Antenna Type (omni or directional)
   Antenna Make and Model
   Antenna Beam Tilt
   Antenna Beam Width
   Antenna Polarization
   For Directional Antennas, Antenna Orientation of Main Horizontal Lobe in Degree of Azimuth with Respect to True North
   For Directional Antennas, Tabulation of Horizontal Plane Relative Field Strengths

Antenna Radiation Center Height Above Ground
Overall Antenna Structure Height Above Ground
Height of Structure Only
Equivalent Isotropically Radiated Power (EIRP)
Site Elevation Above Mean Sea Level
Type of Supporting Structure (*e.g.*, building or tower)
Emission Designator

7. Site Availability Certification

8. Certification of Lack of Environmental Impact (or date of environmental assessment filing with FCC)

9. Service of MDS Application and Interference Study on ITFS Station Licensees with Transmitters within Fifty Miles

10. Carrier Status

11. Legal Entity of Applicant, such as Individual, Partnership, Corporation or Association

12. Preference for Designated Entities under 47 C.F.R. Section 1.2110

13. Ownership and Control of Facilities: Owner, Lessee or Other (identification of any real party in interest, including indirect, future and option interests)

14. Ownership in, Control by, Affiliation with or Lease Arrangement with a Cable Television System and Description of Overlap Between MDS Protected Service Area and Cable Franchise Area; All Communication Interests of the Applicant

15. Financial Ability to Construct and Operate for Twelve Months

16. Description of Any FCC Licenses or Permits Revoked or Applications Denied

17. Issues Relating to Character Qualifications, Including Conviction of a Felony

18. Compliance with Alien Ownership Restrictions of 47 C.F.R. Section 21.4

19. Identification of All Parties Involved in Agreements, or Certification that None Exist, Relating to Any Auction or the Bidding Process

20. Certification of Applicant, Includes Drug Certification

APPENDIX B

Initial Regulatory Flexibility Analysis

Pursuant to the requirements of the Regulatory Flexibility Act of 1980, the Commission finds as follows:

Reason for Action: The Commission is initiating this rulemaking to review and streamline the procedures which govern the filing of applications for new MDS facilities.

Objective: The objective of this proceeding is to improve the Commission's application processes for wireless cable and thereby expedite more service to the public.

Legal Basis: Authority for the action proposed in this proceeding may be found in Sections 4(i) and (j), 301, 303(g) and (r), 309(j) and 403 of the Communications Act of 1934, as amended, 47 U.S.C. Sections 154(i), 154(j), 301, 303(g), 303(r), 309(j) and 403.

Reporting, Recordkeeping and Other Compliance Requirements: The Commission seeks comment on a number of alternative proposals to streamline the procedures for filing new applications for MDS facilities. Generally, the proposed rule changes would reduce the reporting burden on applicants and impose a few new recordkeeping obligations. There may be an additional cost burden to implement the electronic filing proposal.

Federal Rules that Overlap, Duplicate or Conflict with the Proposed Rules: None.

Description, Potential Impact and Number of Small Entities Affected by the Proposed Rules: The Commission believes that the proposals set forth in this proceeding would affect the estimated 500 existing wireless cable operators, many of which are small entities. Adoption of the proposals would benefit small entities interested in acquiring new MDS stations. The proposals would also provide opportunities for equipment manufacturers and video programming providers, many of which may be small businesses. The cost associated with initiating the electronic filing proposal may affect small entities. We are unable to quantify further the potential impact on small entities, and thus, we invite specific comments on this point by interested parties.

Significant Alternatives Minimizing the Impact on Small Entities and Consistent with the Stated Objectives: The *Notice of Proposed Rulemaking* solicits comment on alternatives.

Before the
FEDERAL COMMUNICATIONS COMMISSION FCC 94-295
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Section 309(j)	)	PP Docket No. 93-253
of the Communications Act -	)	
Competitive Bidding	)	

MEMORANDUM OPINION AND ORDER

Adopted: November 16, 1994; Released: November 17, 1994

By the Commission:

I. INTRODUCTION

1. By this action, we reconsider, on our own motion, decisions made in the *Fourth Memorandum Opinion and Order* in this proceeding, which addressed petitions for reconsideration of the *Fifth Report and Order* concerning auction design and procedures for the auction of licenses to provide personal communications services in the 2 GHz band ("broadband PCS").[1] In light of our experience in the national and regional narrowband PCS license auctions, we find it desirable to modify our rules pertaining to three aspects of auction design for the broadband PCS auctions: procedures triggering the close of an auction, timing of the auctions for the entrepreneurs' blocks, and anti-collusion rules.

II. STOPPING RULES

2. In the *Fifth Report and Order* we stated that a simultaneous multiple round auction with a simultaneous stopping rule will close when a single round has passed in which there is no new acceptable bid on any license and no activity rule waiver is submitted.[2] In the *Fourth Memorandum Opinion and Order* we allowed for two types of activity rule waivers, "proactive" waivers, which will keep an auction open in a round in which no new valid bids

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[1] *Fourth Memorandum Opinion and Order* in PP Docket No. 93-253, FCC 94-264 (Rel. October 19, 1994) (*Fourth Memorandum Opinion and Order*); *Fifth Report and Order* in PP Docket No. 93-253, FCC 94-178 (Rel. July 15, 1994) (*Fifth Report and Order*).

[2] *Fifth Report and Order* at ¶¶ 46, 56.

are submitted, and "automatic" waivers, which will not keep an auction open.[3] We also reaffirmed our decision to use a simultaneous stopping rule, which holds bidding open on all licenses until no new acceptable bid is offered on any license.[4] These same rules were applied in the regional and national narrowband auctions. The nationwide narrowband PCS auction (with 10 licenses) was completed after 47 rounds of bidding, and the regional narrowband PCS auction (with 30 licenses) took 105 rounds to complete. In the broadband PCS auctions 99 MTA licenses will be auctioned in the first auction and a total of 1,972 BTA licenses in subsequent auctions. Although the number of rounds to complete a simultaneous multiple round auction is not necessarily directly proportional to the number of licenses put up for bid, we are concerned that, without changes in procedures, it may take an excessively long period of time to conduct these auctions, thus creating a significant delay in providing service to the public.[5] Thus our recent experience with simultaneous multiple round auctions suggests that the Commission should consider additional measures to ensure that future auctions are completed within a reasonable period of time.

3. We believe that retaining the discretion to keep an auction open even if no new acceptable bids and no proactive waivers are submitted will allow the Commission to complete the broadband PCS auctions in a timely manner without sacrificing efficiency or revenue. Providing the auction staff with the discretion to keep an auction open will permit the Commission to use larger minimum bid increments early in the auction (to move the auction along quickly) without incurring the risk that the auction will close while some bidders are willing to pay significantly more for certain licenses than the current high bid but not more than the relatively large minimum bid increments. The Commission will be able to permit additional bidding at lower bid increments subsequent to a round with no bids, thereby increasing the likelihood that licenses will be awarded to the bidders that value them most highly and facilitating efficient aggregations of licenses.

4. Retaining the discretion to keep an auction open will also allow the Commission to continue to accept bids on a license for which a bid was withdrawn late in an auction, especially in the last round of an auction. Without the option of keeping an auction open, a license for which a bid was withdrawn in the last round would have to be put up for bid in a subsequent auction.

5. Accordingly, we retain the discretion to keep an auction open even if no new acceptable bids and no proactive waivers are submitted in a single round. Under this minor modification of our procedures, the Commission would in essence have the ability to submit its own proactive waiver, thus keeping the auction open. This rule modification will facilitate the rapid completion of future auctions because it will permit the Commission to use larger

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[3] *Fourth Memorandum Opinion and Order* at ¶ 15.

[4] *Id.* at ¶ 16.

[5] *Fifth Report and Order* at ¶ 50.

bid increments, which speed the pace of the auction, without risking a premature auction close.

III. TIMING OF AUCTIONS IN THE ENTREPRENEURS' BLOCKS

6. In the *Fifth Report and Order*, the Commission chose to divide broadband PCS licenses into three groups and to hold a simultaneous multiple round auction for the licenses in each group. The license group to be auctioned first consisted of blocks A and B, each with 30 MHz of spectrum and MTA geographic scope. The next group consisted of blocks C and F (the entrepreneurs' blocks), which have been reserved for bidding by smaller entrepreneurial firms. The group to be auctioned last consisted of blocks D and E, with 10 MHz of spectrum each and BTA geographic scope.[6] We concluded that in order to promote efficient license allocation, highly interdependent licenses should be grouped together and put up for bid at the same time in a multiple round auction. Doing so, we concluded, would provide bidders information about the prices of complementary and substitutable licenses while such licenses were still up for bid, and thus would facilitate awarding licenses to the bidders who value them most highly. Nevertheless, we noted that the cost and complexity of auctioning a very large number of interdependent licenses simultaneously might outweigh the informational and bidding flexibility advantages.[7] In the *Fourth Memorandum Opinion and Order* we reaffirmed our decision concerning the sequence of auctions.[8]

7. We now believe that we may wish to hold two separate auctions for the C and F block licenses.[9] In light of our experience with the narrowband auctions, we are concerned that auctioning simultaneously the 986 licenses in the two entrepreneurs' blocks may create excessive administrative complexity for the Commission and for bidders, particularly when neither will have had experience with more than 99 licenses in a single auction. In addition, we have found that as we gain experience with license auctions we identify certain modifications that are necessary to improve the efficiency and administration of the auction process. We may wish to benefit from such experience in administering the highly complex designated entity provisions that apply to competitive bidding for licenses on the C and F blocks. Further, it appears now that few, if any, potential applicants have any interest in

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[6] *Id.* at ¶ 36.

[7] *Id.*

[8] *Fourth Memorandum Opinion and Order* at ¶ 29.

[9] Potential bidders or their representatives have requested that the Commission auction the C and F blocks separately. *See ex parte* comments of the National Association of Black Owned Broadcasters, Inc., filed November 3, 1994 at 2; *ex parte* comments of North American Wireless, Inc., filed November 3, 1994 at 3-4; *ex parte* comments of National Association of Investment Companies, filed November 4, 1994 at 7.

aggregating block C and block F licenses, so that the interdependence between license values in the two blocks may be less than we initially believed. Consequently, we reserve the discretion to hold two separate simultaneous multiple round auctions for the entrepreneurs' block licenses, one auction for block C and one for block F. We will announce by Public Notice in advance of the application deadline whether one or two entrepreneurs' block auctions will be held and the date of those auctions.

IV. ANTI-COLLUSION RULES

8. We have become aware of some confusion regarding the definition of the terms "applicant" and "bidder" as they are used in our anti-collusion rules, and we wish to clarify our rules on this issue.[10] Section 1.2105(c)(1) of the Commission's Rules prohibits "bidders" from cooperating, collaborating, discussing or disclosing in any manner the substance of their bids or bidding strategies, but Section 1.2105(c)(2) and (3) provide exceptions to this rule so as to allow "applicants" to make changes in ownership that do not result in a change in control of the applicant, or to bid jointly with other applicants, as long as they have not applied for licenses in any of the same geographic license areas.[11] Though we intended the terms "bidder" and "applicant" to be used interchangeably, we now recognize that it would be less confusing simply to use the term "applicant," and we are amending the rules accordingly.

9. In addition, it has been suggested that Section 1.2105(c)(1) of our rules should be interpreted to mean that parties holding attributable interests in bidders are not prohibited from engaging in the discussions addressed in that section.[12] We wish to make clear that this interpretation is an incorrect reading of our rules. For purposes of our anti-collusion rules, therefore, we clarify that the term "applicant" will include all holders of attributable interests in an applicant. For this purpose, "attributable interest" shall have the same definition as that used in Section 24.204(d)(2)(i) of our Rules for purposes of defining interests subject to the spectrum aggregation limits: "[p]artnership and other ownership interests and any stock interest amounting to 5 percent or more of the equity, or outstanding stock, or outstanding voting stock of a broadband PCS licensee or applicant will be attributable."[13] In addition, "[o]fficers and directors of a broadband PCS licensee or applicant . . . shall be considered to

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[10] *See* November 4, 1994 letter from Kathy L. Shobert, Director, Federal Affairs, General Communication Incorporated, to William E. Kennard, FCC General Counsel.

[11] *See* 47 C.F.R. § 1.2105(c).

[12] *See* November 4, 1994 letter from James L. Lewis, Vice President, Regulatory Affairs, MCI Telecommunications Corporation to William E. Kennard, FCC General Counsel.

[13] 47 C.F.R. § 24.204(d)(2)(i).

have an attributable interest in the entity with which they are so associated."[14] This is entirely consistent with the intent of the anti-collusion rules. Indeed, if holders of attributable interests were not considered applicants, collusive arrangements would be possible simply through the creation of a separate entity to act as the "applicant." Further, this clarification conforms with other Commission rules regarding the competitive bidding process. For example, Section 24.813(a) requires parties applying to participate in broadband PCS auctions to provide, among other things, information with respect to "any person holding five percent or more of each class of stock, warrants, options or debt securities . . . ."[15]

10. We believe, however, that allowing holders of non-controlling attributable interests in an applicant greater flexibility to form agreements with other applicants may enable applicants to acquire the capital necessary to bid successfully for licenses. Our anti-collusion rules are intended to protect the integrity and robustness of our competitive bidding process. In pursuit of that goal, however, we do not wish to restrict unreasonably the formation of non-collusive bidding consortia. For example, in the *Fourth Memorandum Opinion and Order*, we added to our Rules Section 24.833, which provides that parties that after the auction hold non-controlling ownership interests in more PCS spectrum than a single entity is entitled to hold may divest sufficient properties to come into compliance with the spectrum aggregation limits.[16] Section 24.833 clearly contemplates entities holding ownership interests in two applicants for licenses in the same markets. Nevertheless, when one entity holds an attributable interest in more than one applicant for licenses in the same geographic license area, the potential for collusion is present because of the opportunity for the common owner to influence the bidding of the applicants. Thus, our rules permit applicants to change their ownership, enter into joint bidding arrangements and form consortia after the filing of short-form applications only if the parties to such arrangements have not applied for licenses in any of the same geographic areas.[17]

11. We believe that so long as collusive conduct can be reliably prevented, the public interest favors allowing holders of non-controlling attributable interests in one applicant for a particular license to obtain ownership interests in or enter into consortium arrangements with a second applicant for licenses in the same geographic area(s). Accordingly, we will amend the anti-collusion rules to permit a holder of non-controlling attributable interests in an applicant to obtain an ownership interest in or enter into a consortium arrangement with another applicant for a license in the same geographic area, provided that the attributable interest holder certifies to the Commission that it has observed and will observe certain restrictions on communication concerning the applicants in which it holds an attributable interest or with

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[14] 47 C.F.R. § 24.204(d)(2)(vii).

[15] 47 C.F.R. § 24.813(a)(3).

[16] 47 C.F.R. § 24.833.

[17] 47 C.F.R. § 1.2105(c)(2), (3).

which it has entered into a consortium arrangement. The attributable interest holder must certify that it has not communicated and will not communicate, with the applicant or anyone else, concerning the bids or bidding strategies (including which licenses an applicant will or will not bid on) of more than one applicant for licenses in the same geographic area in which it holds an ownership interest or with which it has a consortium arrangement. As described above, "applicant" for this purpose includes all holders of attributable interests in an applicant. Thus, if the attributable interest holder has discussed the bidding strategy of the applicant in which it holds an attributable interest (Company A), or of any other entity that also holds an attributable interest in Company A, the attributable interest holder may not acquire an attributable interest in another applicant for a license in a geographic area in which Company A (or any other attributable interest holder in Company A) has applied for a license unless it certifies that it has not communicated concerning the bids or bidding strategies of the applicant in which it wishes to acquire an attributable interest.

12. We believe that this revision will facilitate the flow of capital to applicants by enabling parties to make investments in multiple applicants for licenses in the same geographic license areas while ensuring that these investments will not lead to collusion among bidders. We recognize that some potential for collusion exists whenever an entity is permitted to hold an interest in more than one applicant for licenses in the same geographic license area. We expect that the certification requirement will adequately prevent collusion from occurring. However, we intend to scrutinize carefully any instances in which bidding patterns suggest that collusion may be occurring, and we wish to emphasize that all applicants and their owners continue to be subject to existing antitrust laws. Applicants should note that conduct that is permissible under the Commission's Rules may be prohibited by the antitrust laws.[18] Thus, applicants should proceed with extreme caution in situations involving consortia and joint bidding arrangements. We also wish to make clear that communications concerning bids and bidding strategies may include communications regarding capital calls or requests for additional funds in support of bids or bidding strategies to the extent such communications convey information concerning the bids and bidding strategies directly or indirectly. If applicants enter into new or modified consortia or bidding arrangements, or if changes are made in an applicant's ownership, the applicants must timely modify their short-form applications to reflect these changes.

V. ORDERING CLAUSES

13. Accordingly, IT IS ORDERED that Part 1 of the Commission's Rules IS AMENDED as set forth in the attached Appendix.

14. IT IS FURTHER ORDERED that the rule amendments made herein WILL BECOME EFFECTIVE immediately upon publication in the Federal Register. This action is

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[18] *See Fourth Memorandum Opinion and Order* at n.125.

taken pursuant to Sections 4(i), 303(r) and 309(j) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 303(r) and 309(j).[19]

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

[19] Pursuant to 5 U.S.C. § 553(d)(3), we conclude that "good cause" exists to have the rule changes take effect immediately because a delay would not provide applicants with sufficient time to finalize their bidding strategies and business plans for the upcoming broadband PCS auctions. Immediate implementation of the rule changes set forth herein also provides applicants with the required certainty to proceed with their bidding and business strategies, alleviating concerns that last-minute modifications to our Rules would impede the success of their auction plan. *See* 5 U.S.C. § 553(d)(1).

APPENDIX

FINAL RULES

Part 1 of Chapter I of Title 47 of the Code of Federal Regulations is amended as follows:

1. The authority citation for Part 1 continues to read as follows:

AUTHORITY: Secs. 1, 4(i), 303, 309(j), 48 Stat. 1066, 1082, as amended; 47 U.S.C. §§ 151, 154, and 303, unless otherwise noted.

2. The authority citation for subpart Q continues to read as follows:

AUTHORITY: 47 U.S.C. 309(j).

3. Section 1.2105(c) is amended to read as follows:

(c) Prohibition of Collusion.

(1) Except as provided in paragraphs (c)(2), (c)(3) and (c)(4) of this subsection, after the filing of short-form applications, all applicants are prohibited from cooperating, collaborating, discussing or disclosing in any manner the substance of their bids or bidding strategies, or discussing or negotiating settlement agreements, with other applicants until after the high bidder makes the required down payment, unless such applicants are member of a bidding consortium or other joint bidding arrangement identified on the bidder's short-form application pursuant to Section 1.2105(a)(2)(viii).

(2) Applicants may modify their short-form applications to reflect formation of consortia or changes in ownership at any time before of during an auction, provided such changes do no result in a change in control of the applicant, and provided that the parties forming consortia or entering into ownership agreements have not applied for licenses in any of the same geographic license areas. Such changes will not be considered major modifications of the application.

(3) After the filing of short-form applications, applicants may make agreements to bid jointly for licenses, provided the parties to the agreement have not applied for licenses in any of the same geographic license areas.

(4) After the filing of short-form applications, a holder of a non-controlling attributable interest in an entity submitting a short-form application may acquire an ownership interest in, form a consortium with, or enter into a joint bidding arrangement with, other applicants for licenses in the same geographic license area, provided that:

(i) the attributable interest holder certifies to the Commission that it has not communicated and will not communicate with any party concerning the bids or bidding strategies of more than one of the applicants in which it holds an attributable interest, or with which it has a consortium or joint bidding arrangement, and which have applied for licenses in the same geographic license area(s); and

(ii) the arrangements do not result in any change in control of an applicant.

Applicants must modify their short-form applications to reflect any changes in ownership or in the membership of consortia or joint bidding arrangements.

(5) For purposes of this subsection,

(i) the term "applicant" shall include the entity submitting a short-form application to participate in an auction (FCC Form 175), as well as all holders of partnership and other ownership interests and any stock interest amounting to 5 percent or more of the equity, or outstanding stock, or outstanding voting stock of the entity submitting a short-form application, and all officers and directors of that entity; and

(ii) the term "bids or bidding strategies" shall include capital calls or requests for additional funds in support of bids or bidding strategies.

EXAMPLE: Company A is an applicant in area 1. Company B and Company C each own 10 percent of Company A. Company D is an applicant in area 1, area 2, and area 3. Company C is an applicant in area 3. Without violating the Commission's Rules, Company B can enter into a consortium arrangement with Company D or acquire an ownership interest in Company D if Company B certifies either (1) that it has communicated with and will communicate neither with Company A or anyone else concerning Company A's bids or bidding strategy, nor with Company C or anyone else concerning Company C's bids or bidding strategy, or (2) that it has not communicated with and will not communicate with Company D or anyone else concerning Company D's bids or bidding strategy.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

FCC 94-296

In re Petition of MOTOROLA SATELLITE COMMUNICATIONS, INC. for Declaratory Ruling Concerning Participation by COMSAT Corporation in a New Inmarsat Satellite System Designed to Provide Service to Handheld Communications Devices	File No. ISP-94-001

MEMORANDUM OPINION AND ORDER

Adopted: November 17, 1994 Released: November 22, 1994

By the Commission:

1. On October 21, 1993, Motorola Satellite Communications, Inc. ("Motorola") filed a Petition for Declaratory Ruling, urging us to answer the following two questions:

> (1) Does Comsat have the legal authority under the [International Maritime Satellite Telecommunications Act, 47 U.S.C. §§ 751-757,] to provide domestic or international land mobile satellite services over a newly contemplated Inmarsat-P satellite system designed primarily for handheld portable (non-maritime) communications?
>
> (2) Is it in the public and national interest for Comsat to participate in the Inmarsat-P satellite program or for Inmarsat, as an intergovernmental treaty organization, to provide such non-maritime services in the United States in light of the substantial private U.S. commercial interest in developing similar mobile satellite systems?[1]

[1] Motorola Petition for Declaratory Ruling (Oct. 21, 1993) at i.

2. On October 28, 1993, we placed Motorola's petition on public notice. Comments were filed by Motorola, COMSAT Mobile Communications ("COMSAT"), and a wide variety of competitors, equipment manufacturers, and users, both current and potential.[2]

3. After consideration of the International Maritime Satellite Telecommunications Act, 47 U.S.C. §§ 751-757 (the "Maritime Satellite Act"), the Commission's prior interpretations of that Act, and all of the comments filed, we conclude that Motorola's petition should be granted in part and denied in part. *First,* we conclude that it would be premature for us to rule on whether COMSAT's participation in Inmarsat-P would be consistent with the public interest. *Second,* we conclude that if COMSAT's participation in Inmarsat-P takes a form that extends COMSAT's exclusive status within Inmarsat, then it is inconsistent with the Maritime Satellite Act and our prior decisions. If, however, COMSAT's participation in Inmarsat-P takes a form which does *not* extend COMSAT's exclusive status, then such participation would be legally permissible provided it were not inconsistent with COMSAT's statutory maritime mission. We cannot determine whether Inmarsat-P will extend COMSAT's exclusive status until COMSAT files a formal application with us. Accordingly, Motorola's petition is denied in part and granted in part.

I. BACKGROUND

4. The International Maritime Satellite Organization, or Inmarsat, is a treaty-based, intergovernmental organization with seventy-four member nations. Its basic documents, the Inmarsat Convention and Operating Agreement, took effect in July of 1979, with the purpose of providing space segment for global maritime communications via satellite, thereby improving distress and safety communications, public correspondence services, radiodetermination capabilities, and the efficient management of ships.[3] Amendments to the Convention, in force since 1989, extended this purpose to include aeronautical services. More recent amendments, adopted by the Inmarsat Assembly but still

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[2] Comments were filed by the Air Transport Association; American President Lines, Ltd.; Capital Cities/ABC, Inc.; CBS, Inc.; Electronic Equipment Bank; Ellipsat Corp.; Harris Government Aerospace Systems Division; Hughes Aircraft Co.; IDB Mobile Communications, Inc.; Mackay Communications, Inc.; Magnavox Electronic Systems Co.; Manhattan Microwave Communications International, Inc.; Martin Marietta Astro Space, Mobile Telesystems, Inc.; the National Business Aircraft Association, Inc.; the National Telecommunications and Information Administration; National Broadcasting Co., Inc.; Orbital Communications Corp.; OMI Corp.; PanAmSat, L.P.; Princess Cruises; Sea-Land Service, Inc.; Sprint Corp.; Turner Broadcasting System; TRW Inc.; and United Airlines.

[3] *Convention on the International Maritime Satellite Organization (Inmarsat)*, art. 3(1), *reprinted in* INMARSAT BASIC DOCUMENTS (4th ed. 1989) [hereinafter "INMARSAT CONVENTION"]; *In re Communications Satellite Corporation*, 8 F.C.C. Rcd. 638, 638 (1993).

awaiting ratification by the requisite number of member nations, would further extend Inmarsat's mission to the provision of space segment for land mobile communications.[4] The United States is one of the member nations that has already approved these pending amendments to the Inmarsat Convention.

5. In the Inmarsat lexicon, each of the member nations is a "Party." Operational responsibilities within Inmarsat fall not to Parties, however, but to "Signatories." A Signatory *may* be the Party itself, but it may also be some other entity designated by the Party.[5] In each member nation, it is the Signatory, not the Party, that is responsible for financing Inmarsat by contributing the necessary capital. Likewise, it is the Signatory, not the Party, that holds a financial interest in the operations of Inmarsat itself.[6]

6. In the United States, a private corporation is the Inmarsat Signatory. In the Maritime Satellite Act, Congress chose COMSAT as "the *sole* operating entity of the United States for participation in INMARSAT, *for the purpose of providing international maritime satellite communications.*"[7] By virtue of the Convention and the Maritime Satellite Act, COMSAT enjoys a statutory right to be the exclusive provider of Inmarsat space segment to users in the U.S.

7. Since 1991, Inmarsat has been studying the possibility of providing a global, handheld, satellite telephone service to be known as Inmarsat-P. Details of the proposed system have evolved over time. Since at least mid-1993, however, it has been clear that Inmarsat-P would (a) provide voice, facsimile, and data service with global coverage; (b) require a whole new generation of satellites, rather than using the existing or planned Inmarsat satellites; (c) use an "Intermediate Circular Orbit" ("ICO") design, according to which up to fifteen satellites would orbit approximately 10,000 km above the Earth; and (d) service not only maritime users, but also international business travelers, small aircraft, and "quasi-fixed" commercial, industrial, and governmental users in remote areas where there are no terrestrial alternatives.[8]

8. Inmarsat-P was initially planned as a service that would be offered by Inmarsat. However, in May 1994, the Inmarsat Council announced that it would form a separate "Affiliate" which would offer Inmarsat-P service. This Affiliate is to be a private corporation

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[4] INMARSAT CONVENTION, art. 7 "[Amended Text]."

[5] INMARSAT CONVENTION, art. 1.

[6] INMARSAT CONVENTION, art. 5.

[7] 47 U.S.C. § 752(a)(1) (emphasis added).

[8] Motorola Petition for Declaratory Ruling (Oct. 21, 1993), Exhibit 1 (Inmarsat press releases).

without the inter-governmental status provided by the Inmarsat Convention. Inmarsat itself is currently expected to own at least fifteen percent of the Inmarsat Affiliate. Collectively, Inmarsat and its Signatories would own at least seventy percent. Indeed, the initial round of equity financing for the Affiliate would be open only to Inmarsat and its current Signatories. "Strategic investors" are expected to be able to invest in later rounds of financing. Initially, Inmarsat and the Affiliate are expected to enter into contracts for Inmarsat to provide technical support, management, and other services. Inmarsat will also license the Affiliate to use Inmarsat's name and logo, and Inmarsat itself will be the exclusive wholesaler of certain maritime and aeronautical services provided through the Affiliate. The Affiliate is expected to adopt the business plan envisioned all along for Inmarsat-P, using multiple satellites in an ICO orbit and transmitting at frequencies above 2 GHz. COMSAT states that Inmarsat hopes to finalize all investment decisions and create the Affiliate in the next few months, and to commence Inmarsat-P service in 1999 or 2000.

9. Many important features of the Affiliate do not appear in the record before us. For example, the record does not disclose how the Affiliate will be governed; how its retail and wholesale service providers (other than Inmarsat) will be selected; how Inmarsat and its Signatories will be compensated for the research and development work already performed for Inmarsat-P; how Inmarsat will be compensated by the Affiliate for contractual services; or how great Inmarsat's *de facto* influence with the Affiliate will be. Some of these feature have not yet been determined; but even to the extent they have been determined, the relevant corporate documents have not been submitted for the record.

10. Petitioner Motorola is the driving force behind the proposed Iridium satellite system, a low-Earth-orbit (or "LEO") system which would be capable of providing global voice, data, geolocation, paging, and facsimile service through handheld wireless receivers. Motorola filed an application with the Commission in December 1990 for permission to construct the Iridium system; that application is pending. Other companies have also applied to construct "Big LEO" systems -- *i.e.*, LEO systems operating between 1 and 3 GHz. The Big LEO applicants expect to offer services comparable to those planned by Inmarsat-P and are likely to target many of the same potential customers.

II. SUMMARY OF PLEADINGS AND COMMENTS

11. Motorola urges the Commission to declare that COMSAT's participation in Inmarsat-P is foreclosed both as a matter of law and as a matter of policy. On legal grounds, Motorola argues that the Maritime Satellite Act prohibits COMSAT from offering handheld, land-based, mobile satellite service through Inmarsat. On policy grounds, Motorola argues primarily that COMSAT's exclusive relationship with Inmarsat is anticompetitive, and that it would therefore be against public policy to permit COMSAT and Inmarsat to enter a market in which so many U.S. companies wish to compete.

12. To support its legal argument, Motorola relies on our prior interpretations of the Maritime Satellite Act.[9] Motorola argues that under these decisions, we cannot authorize COMSAT to provide non-maritime services unless they are "ancillary to and supportive of" COMSAT's maritime services. According to Motorola, COMSAT's contemplated provision of Inmarsat-P services cannot be approved under this "ancillary and supportive" standard.

13. Motorola also advances a number of policy arguments against COMSAT's provision of Inmarsat-P service in the U.S. According to Motorola, (a) the public interest would not be served by authorizing COMSAT to offer Inmarsat-P service through a non-U.S. satellite system given the presence of private, U.S. corporations willing to provide the same services; (b) allowing COMSAT, and therefore Inmarsat or its Affiliate, to allow Inmarsat-P service in the U.S. will retard the development of competing systems by giving Inmarsat Signatories and other Inmarsat Affiliate investors an incentive to block or delay approval for the Big LEO systems to operate in foreign countries; (c) Inmarsat's "monopoly position" with respect to maritime services could enable it to cross-subsidize Inmarsat-P; and (d) Inmarsat's status as an intergovernmental entity gives it privileges and immunities not enjoyed by private companies, making true competition between Inmarsat-P and Big LEOs impossible. Most of these contentions were first made when Inmarsat itself was expected to offer Inmarsat-P. Motorola now contends that the proposed Affiliate is not sufficiently distinct from Inmarsat to erase the competitive disadvantages the LEOs would face.

14. COMSAT responds to Motorola's legal arguments in two ways. First, COMSAT contends that the Maritime Satellite Act should be read to confer upon COMSAT the power to offer any service permitted by the Inmarsat Convention. COMSAT says that by designating COMSAT as the sole U.S. Signatory to Inmarsat, the Maritime Satellite Act makes COMSAT financially responsible for *all* Inmarsat services, whether they are maritime services, "ancillary and supportive" services, or entirely unrelated services. COMSAT argues that it would have been irrational for Congress to impose unrestricted responsibility on COMSAT while restricting its ability to offer Inmarsat services in the U.S., particularly since Congress knew the Inmarsat Convention could be amended to authorize additional services. Second, COMSAT contends that even if the Maritime Satellite Act limits COMSAT to services that are "ancillary to and supportive of" maritime services, Inmarsat-P meets this standard.

15. COMSAT also takes issue with Motorola's policy arguments. COMSAT points out that the relief originally requested by Motorola would actually *prevent* market entry by a potential competitor to Iridium and the other Big LEOs. COMSAT also claims that (1) Motorola overstates the competitive advantages attributable to Inmarsat's intergovernmental status; (2) in any event, those advantages will not be enjoyed by the Inmarsat Affiliate; (3)

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[9] *In re Communications Satellite Corp.*, 8 F.C.C. Rcd. 638 (1993); *In re Provision of Aeronautical Services via the Inmarsat System*, 4 F.C.C. Rcd. 6072 (1989), *petition for recon. pending*.

Inmarsat-P will create jobs for the U.S., without diminishing the positive economic impact of "U.S." LEOs; (4) Motorola's Iridium system will include foreign governments as investors, so Motorola should not complain about the possibility that Inmarsat-P investors will erect barriers to entry in their home countries; and (5) a decision not to permit COMSAT to offer Inmarsat-P services in the U.S. will be perceived internationally as a protectionist move in favor of the Big LEOs, and may actually exacerbate market-access problems for U.S. telecommunications providers.

16. The majority of the comments we received -- both for and against the Motorola petition -- addressed only the policy issues raised by Motorola. Since we ultimately do not address those policy issues in this proceeding, we need not summarize those comments.

17. Other than Motorola and COMSAT, only Ellipsat Corp., IDB Mobile Communications, Inc., Sprint Corp., and TRW Inc. addressed the legal interpretation of the Maritime Satellite Act. Ellipsat and Sprint offered legal analyses that are essentially indistinguishable from Motorola's. IDB Mobile and TRW, on the other hand, offered significantly different analyses. While these companies agreed with Motorola's argument that Inmarsat-P could not be considered "ancillary to and supportive of" COMSAT's provision of maritime service, both recognized the possibility that COMSAT might be able to offer non-maritime service without meeting the "ancillary and supportive" standard. IDB Mobile, for example, stated that COMSAT could offer Inmarsat-P service "so long as (i) INMARSAT establishes a structurally separate entity to provide INMARSAT-P services and (ii) IDB Mobile and other qualified carriers have the same opportunity to invest in and access such services as Comsat."[10] Similarly, TRW emphasized a "distinction between COMSAT's authority to participate in an Inmarsat program on a monopoly basis, and COMSAT's authority to participate on a non-monopoly basis."[11] TRW asserted that the Maritime Satellite Act, as we have interpreted it, does not prevent us from authorizing COMSAT to "provid[e] non-maritime service, whether via Inmarsat or otherwise, on a non-monopoly basis."[12]

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[10] Comments of IDB Mobile Communications, Inc. (Dec. 8. 1993), at 2. These comments predated the decision of the Inmarsat Council to offer Inmarsat-P through an Inmarsat Affiliate rather than Inmarsat itself. IDB Mobile subsequently took the position that the Affiliate actually proposed was not sufficiently independent of Inmarsat, and did not guarantee that COMSAT would not be the exclusive provider of Inmarsat-P space segment in the U.S. Reply Comments of IDB Mobile Communication, Inc. (July 1, 1994), at 4-7.

[11] Reply Comments of TRW Inc. (Dec. 23, 1993), at 4.

[12] *Id.* at 11. Following COMSAT's disclosure of Inmarsat's decision to create the Affiliate, TRW sated that the Affiliate's "existence as an entity separate from Inmarsat and its monopoly status would be subject to grave doubt." TRW's Response to Supplemental Filing of COMSAT Corporation (June 23, 1994), at 4. TRW also suggested that the unresolved questions regarding the Affiliate made it difficult to determine the extent to which it would be truly separate from Inmarsat. *Id.* at 4-5.

III. DISCUSSION

A. *Propriety and Scope of Declaratory Relief*

18. In its Petition, Motorola urges us to remove the "uncertainty" created by Inmarsat's announced intention to offer land mobile services through Inmarsat-P. Motorola suggests that, because Inmarsat and its Signatories will be making investment decisions on Inmarsat-P in the very near future, and because COMSAT's ability to participate in Inmarsat-P is such an important contingency, Inmarsat, COMSAT, and the other Inmarsat Signatories should not be forced to make their investment decisions without knowing for certain whether COMSAT will be permitted to provide service. Moreover, Motorola further suggests that our decision on COMSAT's ability to participate in Inmarsat-P might influence Inmarsat's resolution of important design and service issues relating to the proposed service. According to Motorola, these conditions make a declaratory ruling appropriate and necessary.

19. We agree that it is appropriate for us to issue a declaratory ruling on the principal legal question raised by Motorola: whether the Maritime Satellite Act permits the Commission to authorize COMSAT to offer Inmarsat-P service through Inmarsat or the Affiliate.[13] In addition to the reasons cited by Motorola, we note that the prospective competitors for land mobile customers in the U.S. and elsewhere are already competitors for capital and for "strategic investors," particularly investors who can make it easier to gain regulatory approvals to operate in key markets overseas. These potential investors, including many Inmarsat Signatories, might well make different decisions about investing in Inmarsat-P depending on COMSAT's ability to participate.

20. We will not, however, decide the policy questions posed by Motorola, for a number of reasons. First, virtually all of the public policy concerns raised in the comments relate not to COMSAT, but to whether Inmarsat's provision of Inmarsat-P services would serve the public interest. Since these policy concerns would be the same even if Inmarsat or the Affiliate chose an entity other than COMSAT as the wholesaler for Inmarsat-P services in the U.S., we think they form an inappropriate basis for a declaratory ruling on COMSAT's ability to participate in Inmarsat-P.

21. Second, many of the policy issues raised here are not unique to this particular service offering or even this particular industry. The danger that Inmarsat might cross-subsidize the Affiliate's Inmarsat-P services, for example, is just one instance of an economic danger that we have faced in other areas. At the licensing stage, we can often mitigate such

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[13] *See* 47 C.F.R. § 1.2 (1993). We do not address a separate legal issue, namely whether the Inmarsat Convention allows *Inmarsat* to offer Inmarsat-P service, through Comsat or any other entity. This issue (along with the related issue of whether the proposed "Inmarsat Affiliate" would itself be subject to any restrictions in the Inmarsat Convention) is committed primarily to the judgment of the Executive Branch, which is examining these questions now.

dangers by imposing appropriate conditions on the license. The competitive concerns raised by Motorola might well be amenable to such treatment, enabling the Commission to allow the Affiliate into the mobile satellite services market on conditions that would truly make the new entry pro-competitive. For this reason, we would prefer to confront such regulatory issues in that more flexible and customary manner, based on a specific proposal, with a formal application before us.[14]

22. Finally, many of Motorola's policy concerns are currently being considered by the Executive Branch. The Maritime Satellite Act gives the President broad authority to supervise and instruct COMSAT in its Inmarsat-related activities, to ensure that COMSAT acts in harmony with "the national interest and foreign policy of the United States."[15] The broad policy issues raised by Motorola should be considered in this wider context. We therefore deny Motorola's Petition to the extent that it requests a declaration that any COMSAT participation in Inmarsat-P would be contrary to the public interest. We address only the legal question of whether the Maritime Satellite Act permits us to authorize Comsat to offer Inmarsat-P service through Inmarsat or an Affiliate.

23. Our deferral of Motorola's competitive concerns does not mean we view these issues as relatively less important. We are committed to full and fair competition wherever feasible, and if and when we receive an application for authority to provide Inmarsat-P service in the U.S., we will scrutinize that application to determine whether it is in the public interest, taking full account of any potential anti-competitive effects.

B. The Scope of COMSAT's Legal Authority

24. Motorola bases its legal argument on a number of previous decisions made when Inmarsat has expanded into new modes of service. A little history provides the proper context for this legal argument. In 1987, we ruled that the Maritime Satellite Act did not permit us to authorize COMSAT to provide non-maritime services through Inmarsat, and we therefore denied COMSAT's application to provide aeronautical services in the U.S. *In re Communications Satellite Corp.*, 2 F.C.C. Rcd. 390 (1987) ("*Aeronautical Services Order I*"), *vacated*, 4 F.C.C. Rcd. 6072, 6088 (1989). Two months later, we initiated a rulemaking to

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[14] In addition, working groups within Inmarsat are currently considering significant questions not only about the nature of the Affiliate, but about the nature of Inmarsat itself. Our consideration of Motorola's policy concerns might be quite different if, for example, Inmarsat were transformed into a private corporation, or if the Convention were amended to allow multiple signatories or greater direct access. Because Inmarsat is likely to resolve some of these questions long before 1999 or 2000, we can take better account of the possibilities by deferring our consideration of the relevant policy issues until a formal application is filed.

[15] 47 U.S.C. § 753(b).

determine how aeronautical services via Inmarsat should be provided in the U.S.[16] The comments received persuaded us, in "*Aeronautical Services Order II*,"[17] to vacate *Aeronautical Services Order I* and modify our earlier conclusion that the Maritime Satellite Act flatly prohibited COMSAT from offering aeronautical services via Inmarsat.

25. In *Aeronautical Services Order II*, we summarized the anti-monopoly reasoning of *Aeronautical Services Order I*[18] and then stated, "We continue to conclude that Comsat's express authorization is limited to maritime services."[19] However, we also observed that the Maritime Satellite Act did not expressly prohibit COMSAT from providing non-maritime services through Inmarsat; and in the face of this legislative silence we held that the Act should be construed to authorize non-maritime services that are "ancillary to and supportive of" maritime services.[20] On the record before us in *Aeronautical Services Order II*, we determined that Comsat had satisfied this standard and that it should therefore be permitted to provide aeronautical services notwithstanding the lack of any express authorization of such services in the Maritime Satellite Act.[21]

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[16] *In re Provision of Aeronautical Services via the INMARSAT System*, 2 F.C.C. Rcd. 1976 (1987).

[17] *In re Provision of Aeronautical Services via the INMARSAT System*, 4 F.C.C. Rcd. 6072 (1989), *petitions for recon. pending.*

[18] In *Aeronautical Services Order I,* we had stated,

> [W]e find that the Maritime Satellite Act does not permit us to authorize Comsat to participate in aeronautical services via INMARSAT on a monopoly basis. We conclude that the Act confers a monopoly status on Comsat that is limited to the provision of maritime satellite services, and that the legislative history of the Act clearly shows that Congress intended Comsat's monopoly role in INMARSAT to be so limited. We believe that any extension of Comsat's monopoly status in providing INMARSAT services must consider the effect that this would have on the potential for competition in aeronautical services. In view of the fact that Comsat's monopoly in providing maritime services via INMARSAT was conferred on it by legislative action, we believe that its extension to these services can only be granted by similar action.

2 F.C.C. Rcd. at 394.

[19] 4 F.C.C. Rcd. at 6085.

[20] 4 F.C.C. Rcd. at 6084-86.

[21] 4 F.C.C. Rcd. at 6086-87.

26. In this proceeding, COMSAT first contends that the Maritime Satellite Act permits it to offer any type of service offered by Inmarsat itself. In so contending, COMSAT relies most heavily upon the fact that the Maritime Satellite Act imposes a number of obligations upon COMSAT with no apparent restriction to maritime services. For example, the Act states that its purpose is "to provide that the participation of the United States in INMARSAT shall be through [COMSAT]," without expressly limiting such participation to maritime services.[22] Likewise, the Act authorizes COMSAT to "participate in and . . . sign the operating agreement or other pertinent instruments of Inmarsat as the sole designated operating entity of the United States,"[23] and to "establish, own, and operate the United States share of the jointly owned international space segment and associated ancillary facilities,"[24] again without any express limitation to maritime services. Finally, the Act states that COMSAT "shall be the sole United States representative in the managing body of INMARSAT," and shall "fulfill[] any financial obligation placed upon the corporation as a signatory to the operating agreement or other pertinent instruments, [or] as the result of a convention or other instrument establishing INMARSAT."[25] COMSAT further contends that nothing in the Act relieves COMSAT of these obligations with respect to non-maritime services. COMSAT concedes that other provisions of the Act do specifically refer to maritime services. Section 502, for example, "declares that it is the policy of the Unites States to provide for the participation of the United States in [Inmarsat] *in order to develop and operate a global maritime satellite telecommunications system.*"[26] However, COMSAT argues that these provisions lack any sense of limitation, and must therefore be interpreted as illustrative only. In short, COMSAT argues that the specific, nuts-and-bolts provisions about who represents the United States government (apparently even on non-maritime matters) and who pays for Inmarsat operations (apparently even non-maritime operations) must control the broader provisions of the Act which mention and clearly contemplate maritime services but do not by their terms rule out non-maritime services.

27. COMSAT also disagrees with the way we have interpreted the legislative history behind the Maritime Satellite Act.[27] COMSAT notes that when the Maritime Satellite

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[22] 47 U.S.C. § 751(b).

[23] 47 U.S.C. § 752(a)(3).

[24] 47 U.S.C. § 752(c)(4).

[25] 47 U.S.C. § 752(d).

[26] 47 U.S.C. § 751(a) (emphasis added).

[27] In both *Aeronautical Services Order I* and *Aeronautical Services Order II*, we quoted a portion of the House Report, which reads as follows:

> This Committee does not intend that H.R. 11209 give Comsat a monopoly in an international satellite system. *H.R. 11209 relates solely to*

Act was enacted, COMSAT had already been the sole U.S. Signatory to Intelsat for more than fifteen years, and some were concerned that by designating COMSAT as the U.S. Signatory for a second international satellite organization (Inmarsat), Congress would be setting a precedent that would make COMSAT the prohibitive favorite for selection as Signatory to any additional international satellite organizations that might be created. According to COMSAT, the true meaning of the legislative history is merely that no such prejudgment of COMSAT's role in any future international satellite organization was intended. Indeed, COMSAT asserts that our 1987 analysis of this legislative history was not repeated in our 1989 decision in *Aeronautical Services Order II*, and suggests that this is because the Commission in 1989 "recogniz[ed] its error."

28. These arguments have been considered and rejected in our past decisions. We reject them again today. Our fundamental premise is that competition is to be favored and restrictions on competition disfavored. The Maritime Satellite Act confers upon COMSAT an exclusive dealing arrangement with Inmarsat that is a departure from purely competitive principles.[28] Because Congress granted this statutory right of exclusivity "for the purpose of

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> *maritime satellite telecommunications services* and does preclude [*sic* -- *probably should be "does not preclude"*] the designation of some other entity for other international satellite systems that may be developed in the future. The Congress will have to look at those systems when they are proposed. Further, this Committee does not intend that H.R. 11209, which relates solely to international maritime satellite telecommunications services, inhibit the Federal Communications Commission (FCC) from authorizing domestic satellite systems to serve the interests of the maritime community.

H.R. Rep. No. 95-1134, 95th Cong., 2d Sess., at 10 (emphasis added). We also quoted a portion of the following paragraph from the Senate Report:

> By designating Comsat to represent the United States in providing international maritime satellite communications, *the committee does not intend to authorize Comsat to provide other international communications services not contemplated by this bill.* If other international telecommunications services become feasible in the future, the committee will examine the provision of those services on the information then available. Action taken by the committee in this instance would not necessarily be a precedent for management of future international telecommunications systems.

S. Rep. No. 95-1036, 95th Cong., 2d Sess., at 8 (emphasis added).

[28] It is this right of exclusive dealing which we have previously characterized as a "monopoly." *See, e.g., Aeronautical Services Order II*, 4 F.C.C. Rcd. at 6084-85. The use of the word "monopoly" is somewhat problematic in the current context, since all parties to this proceeding strongly believe that consumers in the U.S. will be able to purchase handheld land mobile satellite services from many suppliers, with space segment provided by at least five different satellite systems, even if neither COMSAT nor Inmarsat enters this market. In such

providing international maritime satellite telecommunications services,"[29] we have held that COMSAT's provision of Inmarsat services "on a monopoly basis" is limited to maritime services and whatever other services are "ancillary to and supportive of [COMSAT's] provision of maritime services."[30] We reaffirm that holding today.

29. This conclusion is supported by the legislative history of the Act. The overriding purpose of the Maritime Satellite Act was "the establishment, ownership, operation, and governmental oversight and regulation of international maritime telecommunications services."[31] Moreover, the House and Senate Reports both limit the Act to maritime "services," not maritime "systems."[32] And while it is true that some observers expressed concern about COMSAT's place in future international satellite systems, that fact is in no way inconsistent with the view that Congress was also concerned with COMSAT's provision of non-maritime services within the Inmarsat system. The Senate Report, in particular, lends itself to the interpretation that Congress meant both to limit COMSAT's Inmarsat "monopoly" to maritime services *and* to disclaim any intention to make COMSAT the U.S. Signatory in any future international satellite organizations.[33] In the absence of new arguments, authorities, or circumstances, we hold once again that if COMSAT's exclusive relationship with Inmarsat is to be extended beyond maritime services (or services that are ancillary to and supportive of maritime services), that extension must come from a direct command of Congress.

30. COMSAT's second major legal argument is that its participation in Inmarsat-P can be reconciled with the Maritime Satellite Act because Inmarsat-P service would be "ancillary to and supportive of" COMSAT's provision of Inmarsat's traditional maritime service. Motorola urges us to reject this argument because the factual criteria we have used

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a market, COMSAT clearly would not have a "monopoly" in the strict sense, but it would have an exclusive right to provide services via one particular satellite system -- Inmarsat's. We therefore prefer to characterize COMSAT's status as an statutorily granted exclusive right of dealing, or a statutory right of exclusivity, rather than a monopoly.

[29] 47 U.S.C. § 752(a)(1). *Accord*, 47 U.S.C. § 751(a) (policy of the U.S. is to participate in Inmarsat "in order to develop and operate a global maritime satellite telecommunications system," which will "serve maritime commercial and safety needs").

[30] *Aeronautical Services Order II*, 4 F.C.C. Rcd. at 6085.

[31] H.R. Rep. No. 95-1134, 95th Cong., 2d Sess., at 5; S. Rep. No. 95-1036, 95th Cong., 2d Sess., at 1.

[32] H.R. Rep. No. 95-1134, 95th Cong., 2d Sess., at 10.; S. Rep. No. 95-1036, 95th Cong., 2d Sess., at 8.

[33] *See* S. Rep. No. 95-1036, 95th Cong., 2d Sess., at 8 (mentioning both systems and services).

to evaluate "ancillarity" and "supportiveness" in the past do not permit the conclusion that Inmarsat-P would be "ancillary and supportive." COMSAT responds that the three criteria to which we have referred in the past are not the only conceivable means by which ancillarity and supportiveness might be measured, and that in any event those three criteria do demonstrate that Inmarsat-P would be ancillary to and supportive of COMSAT's provision of maritime services via Inmarsat.

31. In *Aeronautical Service Order II*, after stating our "conclusion that Comsat's provision of aeronautical services would be ancillary to and supportive of its provision of maritime services,"[34] we stated:

> The critical factors supporting this conclusion are: (1) aeronautical services will be subsidiary to maritime services which will remain Inmarsat's primary mission; (2) aeronautical and maritime services will be provided over common space satellite resources and ground facilities and will use both common and contiguous spectrum; and (3) the resulting integrated operation of aeronautical and maritime services will not permit Inmarsat Council decisions regarding the planning and use of space segment to be separated in terms of aeronautical and maritime services.[35]

32. Since we decided *Aeronautical Services Order II*, we have had one other occasion to apply the "ancillary to and supportive of" standard. On that occasion we did indeed justify our conclusion with reference to the same three "critical factors" we discussed in *Aeronautical Services Order II*, and referred to those factors as "the criteria established" in *Aeronautical Services Order II*.[36] Nonetheless, we agree with COMSAT that Motorola goes too far in characterizing our discussion of these factors as a "three-part test." Although they were "critical" in that case, we have never suggested that these three factors exhaust the meaning of ancillarity or supportiveness. Whether a proposed service is "ancillary to and supportive of" existing Inmarsat maritime service is not a matter of checking off boxes. It is rather a matter of practical judgment, conducted case by case upon all of the facts.[37] As we

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[34] 4 F.C.C. Rcd. at 6086.

[35] 4 F.C.C. Rcd. at 6086.

[36] *In re Communications Satellite Corp.*, 8 F.C.C. Rcd. 638, 641-42 (1993) (granting COMSAT's application for authority to provide international land mobile satellite services outside North America).

[37] Indeed, the considerations that lead us to construe our precedent in this fashion are so powerful that, if our precedent had endorsed an exhaustive "three-part test," we would reject our precedent to the extent it conflicts with our decision here.

said in *Aeronautical Services Order II*, the "ancillary and supportive" determination turns on "whether Comsat's provision of [the service in question] is closely related to and important to protect or promote either its provision of maritime satellite services or its participation in Inmarsat decisions regarding maritime services."[38] Our judgment is also informed by the Supreme Court's observation that "[w]hatever may fairly be regarded as incidental to, or consequential upon, those things which the legislature has authorized, ought not, unless expressly prohibited, to be held, by judicial construction, to be *ultra vires*."[39]

33. Motorola argues that COMSAT's provision of land-based, mobile satellite services through Inmarsat-P cannot be considered "ancillary to and supportive of" COMSAT's provision of Inmarsat maritime services for a number of reasons. Foremost among them is the sheer size of the contemplated Inmarsat-P service, in terms both of customers and of capital investment. Motorola notes that Inmarsat-P services are expected to require an entirely new generation of satellites, a different portion of the spectrum, and separate gateway earth station facilities. Motorola estimates the cost of Inmarsat-P to be in excess of $2 billion, a figure that "would exceed by a considerable margin the total cost Inmarsat has incurred to date for all of its satellite and ground facilities."[40] Finally, Motorola argues that, especially in light of the proposed offering of Inmarsat-P through a separate "Inmarsat Affiliate," operational decisions regarding Inmarsat-P will be easily separable from Inmarsat's operational decisions pertaining to maritime services.

34. COMSAT responds to Motorola's arguments by emphasizing that Inmarsat-P will be used by maritime as well as non-maritime subscribers; and that although non-maritime subscribers may predominate, that fact alone does not preclude our finding the service to be ancillary to other maritime services. Indeed, COMSAT asserts that land-based users are expected to account for 75% of Inmarsat's total traffic by the year 2000 even without Inmarsat-P. The important inquiry, according to COMSAT, is not whether non-maritime users outnumber maritime users, but whether maritime users are adequately served. COMSAT claims that Inmarsat-P will improve service to maritime users, and that maritime services will always be Inmarsat's first priority because the Inmarsat Convention requires this. Moreover, COMSAT claims that while Inmarsat-P will require separate space and ground segment from that used by Inmarsat at present, it is nonetheless true that Inmarsat-P will "by its nature . . . entail integrated operation of maritime, aeronautical and land mobile services, which will enable COMSAT to provide Inmarsat-P service to maritime users on an efficient

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[38] 4 F.C.C. Rcd. at 6086.

[39] *Jacksonville, Mayport, Pablo Railway and Navigation Co. v. Hooper*, 160 U.S. 514, 525 (1896) (*quoted in Aeronautical Services Order II*, 4 F.C.C. Rcd. at 6085-86).

[40] Motorola Petition for Declaratory Ruling (Oct. 21, 1993), at 24.

and cost-effective basis."[41] COMSAT also contends that because many users of Inmarsat-P will be maritime users, COMSAT cannot carry out its responsibilities to maritime users without being involved in operational decisions regarding Inmarsat-P.

35. COMSAT's final argument relates not to the "critical factors" we have previously identified, nor to Motorola's specific arguments, but rather to the future of the market for satellite services. COMSAT points out that Motorola's Iridium system, and presumably the other LEOs as well, will certainly not confine their marketing efforts to land-based users. In all likelihood, they will aggressively pursue maritime customers, many of whom may currently use Inmarsat's "traditional maritime service." There is, then, in COMSAT's words, "no separate market for 'handheld' or 'land-based' service."[42] Thus, COMSAT contends that it (and Inmarsat) cannot effectively provide the global maritime services COMSAT is statutorily charged with providing unless Inmarsat is permitted to let its services "evolve" in response to the absorption of its "traditional maritime" market into a larger market for mobile satellite services.

36. COMSAT's attempt to satisfy the "ancillary and supportive" standard is, in our view, compromised by Inmarsat's decision that Inmarsat-P service should be offered by the Affiliate. Given the proposed institutional separation between Inmarsat and the Affiliate, we cannot accept COMSAT's characterization of Inmarsat-P as merely a logical, evolutionary update of Inmarsat's traditional maritime service. COMSAT may be correct in asserting that maritime users would benefit from the introduction of Inmarsat-P, and that Iridium and the other Big LEOs will attempt to lure these users away from Inmarsat. But as long as Inmarsat-P is offered through a separate Affiliate, we must regard that Affiliate not as "ancillary and supportive," but as one more competitor of Inmarsat's traditional maritime service. In short, we cannot see how, under the proposed arrangement, *Inmarsat's existing maritime service* would be any more viable with Inmarsat-P than without it. It follows that COMSAT's provision of Inmarsat-P cannot "fairly be regarded as incidental to, or consequential upon," COMSAT's statutory obligations toward Inmarsat.

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[41] Opposition of COMSAT Corporation to Petition for Declaratory Ruling (Dec. 8, 1993), at 16.

[42] Opposition of COMSAT Corporation to Petition for Declaratory Ruling (Dec. 8, 1993), at 36.

> The simple fact of the matter is that communications satellites do not normally distinguish between locations of users on land, at sea or in the air. Nor will users of handheld global satellite services willingly limit where they use those services. Absent artificial regulatory restraints (which would in any event be extremely difficult to enforce), users will carry their handheld (dual mode) receivers from their homes to their offices to their boats, as well as on business trips to remote areas.

Id.

37. Nor are we persuaded to the contrary by the fact that Inmarsat is expected to be the exclusive wholesaler of some Inmarsat-P services to maritime and aeronautical customers. In the first place, true ancillarity cannot be based on the bare fact that Inmarsat would benefit in some way. Inmarsat might benefit from many ventures that would in no way be "ancillary" to its maritime services; and Inmarsat's "evolution" into a wholesaler of space segment on a non-Inmarsat system, no matter how beneficial, would clearly be a brand new business -- not something on the edges of the old one. Second, we reiterate that our primary focus must always be on COMSAT, because the Maritime Satellite Act gives us regulatory authority over COMSAT, not Inmarsat. Consequently, in applying our "ancillary and supportive" standard we must ask whether *COMSAT's* provision of non-maritime services is reasonably ancillary to *COMSAT's* effective discharge of its statutory obligations toward Inmarsat and toward maritime users. We acknowledge that the link between *Inmarsat's* non-maritime activities and *Inmarsat's* traditional maritime services may often be an important consideration. For example, when Inmarsat acts in its traditional capacity as the system over which space segment is provided (as in *Aeronautical Services Order II*), Inmarsat's need to move into a new area tends to imply its Signatories' needs to move with it, for the Signatories are operationally involved. Here, however, Inmarsat will benefit from Inmarsat-P not as the *system*, but as just another wholesaler. We see no operational connection between Inmarsat's need or ability to fill this role and COMSAT's independent participation as another wholesaler.

38. Furthermore, Inmarsat-P services cannot be characterized as ancillary because by any reasonable measure, Inmarsat-P is expected to become the very large tail of a relatively small dog. Inmarsat projects that by 2010 Inmarsat-P will reach over 3,000,000 subscribers, of whom more than 2,500,000 will be land-based rather than maritime.[43] This amounts to roughly a fifty-fold increase over Inmarsat's current subscribership, and a much greater increase in the volume of non-maritime traffic. COMSAT's participation in such a robust expansion cannot reasonably be called "ancillary to and supportive of" COMSAT's provision of Inmarsat maritime services. This is particularly true since Inmarsat-P is expected to use different (and much costlier) satellites and ground facilities, as well as different (and non-contiguous) spectrum.

39. Finally, we would reach the same conclusion if Inmarsat itself intended to provide Inmarsat-P services. COMSAT has conceded that the maritime aspects of Inmarsat-P would not, alone, be sufficient to justify the huge capital outlays that will be required to provide Inmarsat-P. This fact would make it impossible for us to conclude that the non-maritime aspects of Inmarsat-P were merely "incidental" to the maritime aspects of Inmarsat-P, let alone Inmarsat's other maritime services. We would reach this conclusion even if the maritime and non-maritime elements of the new service used the same space and ground facilities and the same spectrum, and even if the maritime and non-maritime services were

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[43] Motorola's Reply Comments in Support of Petition for Declaratory Ruling (Dec. 23, 1993), at 14.

operationally integrated. We therefore conclude that COMSAT's proposed provision of Inmarsat-P service through the Affiliate would not be "ancillary to and supportive of" COMSAT's provision of Inmarsat's core maritime service.

40. The analysis to this point has led us through several intermediate conclusions: (a) that the Maritime Satellite Act generally does not permit us to authorize COMSAT to offer non-maritime services through Inmarsat on an exclusive basis; (b) that COMSAT may nonetheless offer such services, consistent with the Maritime Satellite Act, to the extent that they are "ancillary to and supportive of" COMSAT's provision of maritime services through Inmarsat; but (c) that Inmarsat-P, as currently proposed, cannot satisfy this "ancillary and supportive" standard. However, it bears repeating that COMSAT does not currently have any application before us. Thus, Motorola has not asked us to deny an application by COMSAT to provide Inmarsat-P service in the U.S.; rather it has asked us to declare that COMSAT may never, under any circumstances, offer Inmarsat-P service in the U.S. under the Maritime Satellite Act. This broader request requires us to continue our analysis and discuss the limits of the restrictions imposed on COMSAT by the Maritime Satellite Act.

41. Our decision in *Aeronautical Services Order I* was not our first attempt to define the extent to which the Maritime Satellite Act limits COMSAT's ability to engage in new lines of business. Seven years earlier, we completed our "*COMSAT Study*,"[44] a comprehensive report on COMSAT which we were required to conduct under the Maritime Satellite Act.[45] One of the "policy problems" we identified in that *Study* was the increasing desire of COMSAT, which since 1962 had been the U.S. Signatory to Intelsat, to move into non-Intelsat lines of business. We recognized that this desire was in large part a consequence of the fact that "Comsat's primary mission under the 1962 Act -- to marshall U.S. space technology for the purpose of establishing a global communications satellite system in conjunction and cooperation with other countries -- has been largely accomplished through the successful development of the INTELSAT global system."[46] We thus undertook a detailed consideration of COMSAT's "Scope of Authority" to engage in these non-Intelsat (and, looking forward, non-Inmarsat) lines of business.

42. In our *COMSAT Study*, we noted that COMSAT, though legislatively created, nonetheless possesses almost all the powers normally exercised by a District of Columbia corporation. We continued:

> The [Communications Satellite Act of 1962, as amended] and Comsat's Articles of Incorporation make it clear that Comsat

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[44] *In re Comsat Study -- Implementation of Section 505 of the International Maritime Satellite Telecommunications Act*, 77 F.C.C.2d 564 (1980).

[45] 47 U.S.C. § 754.

[46] 77 F.C.C.2d at 607.

> *must* engage in activities that are necessary to establish the global system contemplated by Section 102 [of the 1962 Act]. By the same token, Comsat may *not* engage in activities that are inconsistent with its statutory mission or will interfere with or hinder realization of the Act's purposes and objectives. *As to other activities, the Act and the Articles of Incorporation are neutral.* We therefore believe that there is no legal bar either in the Act or the Articles to activities that do not necessarily further the global system, *so long as such activities are not inconsistent with, and do not hinder or interfere with the Act's purposes and objectives.*[47]

43. In *Aeronautical Services Order I*, COMSAT urged us to approve its applications under the standard set forth in our *COMSAT Study*. We declined to do so, pointing out,

> The analysis in the *Comsat Study* did not address the scope of Comsat's congressional mandate under the Maritime Satellite Act to provide services via INMARSAT on a monopoly basis. Rather it focused on the scope of Comsat's authority to engage in competitive, non-INTELSAT and non-INMARSAT activities. Our *Comsat Study* therefore cannot be controlling on the issue of aeronautical services via INMARSAT.[48]

Although we later vacated *Aeronautical Service Order I*, we continue to believe that the standard set forth in our *COMSAT Study* does not apply when COMSAT seeks to provide services via Inmarsat or Intelsat. Nonetheless, COMSAT's proposal to provide Inmarsat-P services through the "Inmarsat Affiliate" raises the possibility that the less restrictive standard set forth in the *COMSAT Study* may apply to any COMSAT application to provide Inmarsat-P services through an entity separate and distinct from Inmarsat.

44. Under the "not inconsistent" standard set forth in our *COMSAT Study*, COMSAT could conceivably provide handheld, land-based, mobile satellite services consistent with the Maritime Satellite Act. It could do so, for example, by launching its own satellite system, entirely independent of Inmarsat or Intelsat; or by investing in a Big LEO system and becoming a service provider for that system. These "non-Intelsat, non-Inmarsat" lines of business would be evaluated under the "not inconsistent" standard we announced in 1980.

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[47] *COMSAT Study*, 77 F.C.C.2d at 615 (citations and footnotes omitted; emphasis added).

[48] *Aeronautical Services Order I*, 2 F.C.C. Rcd. at 394.

45. The question here is whether Inmarsat-P would truly be a "non-Inmarsat" venture. According to the latest publicly available information, Inmarsat will directly own 15% of the Affiliate; Inmarsat and its Signatories, collectively, will own a majority of the Affiliate's stock, at least 70%; Inmarsat will provide operational support to the Affiliate and act as a wholesaler; and the Affiliate will operate under the Inmarsat name and logo. In light of these facts, we must consider whether COMSAT's participation in such an entity can be considered a "non-Inmarsat" line of business.

46. In answering this question, we turn once again to our *COMSAT Study*. There, we stated,

> Our concern with the effect the application of Comsat's technology and expertise may have on competitive marketplaces is based on two factors: (1) the substantial monopoly powers and privileges Comsat enjoys under the 1962 Act, and (2) the fact that Comsat developed the technology and expertise that it now seeks to commercially exploit primarily by virtue of its special INTELSAT role and with the aid of early taxpayer-funded technology developed by NASA. We believe that Comsat should not be permitted to utilize its *status as the U.S. representative in INTELSAT and INMARSAT* to gain competitive advantages in technology development or other markets, which will tend to discourage vigorous competition in these markets.[49]

47. Following our *COMSAT Study*, we believe that COMSAT's "status as the U.S. representative in INTELSAT and INMARSAT" is the key to distinguishing between businesses that are related to Intelsat or Inmarsat and businesses that are not. If a business venture proposed by COMSAT would *extend COMSAT's statutory exclusive status within Inmarsat,* we will evaluate it under the "ancillary and supportive" standard we have applied since *Aeronautical Services Order II.* If, however, the line of business proposed by COMSAT is one which could be entered by any similarly disposed and similarly qualified private firm, then our historical concerns about extending COMSAT's "monopoly" lose their force. We will therefore treat any such business venture as a "non-Intelsat, non-Inmarsat" venture, and evaluate it under the "not inconsistent" standard we announced in 1980.

48. As we have said, the nature of the proposed Affiliate is not entirely clear from the record. This prevents us from passing judgment now on whether the Affiliate, as proposed, would qualify as a "non-Inmarsat" venture. However, three observations cast further light on what will be considered "non-Inmarsat" and therefore outside the Maritime Satellite Act.

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[49] *COMSAT Study*, 77 F.C.C.2d at 609.

49. First, by focusing on the extent to which the new venture *extends COMSAT's statutory right of exclusivity*, we deliberately do not employ more familiar common-law phrases like "piercing the veil" or "*alter ego*." Our test is not based primarily on corporate relationships, controlling interests, interlocking directorates, or the use of logos and trademarks *per se*. These details may be relevant insofar as they have real-world, competitive consequences, but they are not necessarily dispositive and may not be very important in light of all the circumstances.

50. Second, because our test is designed to prevent extension of an exclusive relationship, we think it relevant to examine not only who participates, but who is not permitted to do so. Thus, a venture that were open to the participation of a suitable cross-section of non-Signatory telecommunications entities and other investors would not, in our view, necessarily be irremediably tainted merely because Inmarsat or certain individual Signatories happened also to have viewed it as a promising business opportunity. By contrast (to take an extreme case), if participation in the new venture were restricted to Inmarsat and its Signatories, it would be impossible for us to conclude that COMSAT were participating in a non-Inmarsat venture.

51. Third, and perhaps most importantly, the competitive focus of our test will require us to examine a proposed venture's operational principles as well as its finances, to see whether any special privilege is directly or indirectly attached to Signatory status *per se*. For example, any venture structured so as to guarantee that COMSAT, *strictly by virtue of its status as an Inmarsat Signatory*, exercises exclusive control over the availability of space segment, would appear on its face to constitute an extension of COMSAT's exclusive status within Inmarsat, and would therefore be regulated under the Maritime Satellite Act.

52. These three observations should not be construed as a "three-part test" for determining whether a proposed business venture by COMSAT is an Inmarsat business or a non-Inmarsat business. There is only one test: whether the proposed venture, viewed as a whole, effectively extends COMSAT's statutory exclusive relationship with Inmarsat. Because the test is a unitary one, it should be equally clear that the Commission's decision might, in a future case, rest upon any combination of the considerations we have discussed, or upon others.[50]

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[50] We note in particular that all of the considerations discussed in the text are relevant within the context of an intergovernmental Inmarsat in which COMSAT is the sole U.S. Signatory. If the current debates within Inmarsat lead to fundamental changes in that organization's structure, or if Congress determines to modify COMSAT's exclusive dealing arrangement with Inmarsat, some of the factors we discuss might become less important or irrelevant altogether.

Motorola and several commenters have urged us to adopt specific conditions which must be met before COMSAT can offer Inmarsat-P service through the Affiliate. *See, e.g.*, Motorola's Comments on the Proposed Inmarsat Affiliate (June 23, 1994); Supplemental

53. We cannot, as Motorola requests, declare that the Maritime Satellite Act absolutely bars COMSAT from providing Inmarsat-P service through the Affiliate. We can indeed conceive of circumstances under which an Affiliate would be sufficiently distinct from Inmarsat to qualify as a "non-Inmarsat" line of business. COMSAT's proposed participation in such a venture would be evaluated under the "not inconsistent" standard of our *COMSAT Study*. Motorola's Petition is therefore denied to this extent. However, because the record does not reflect the form the proposed Affiliate might ultimately take, it is also entirely possible that the Affiliate will be structured in such a way as to extend COMSAT's statutory right of exclusivity beyond the scope contemplated by the Maritime Satellite Act. In that case, COMSAT's participation in the Affiliate would be prohibited by the Maritime Satellite Act unless it were "ancillary to and supportive of" COMSAT's provision of maritime services through Inmarsat; and we have indicated that Inmarsat-P, as currently proposed, could not satisfy this "ancillary and supportive" standard. Thus, Motorola's Petition, to this extent, is granted.

CONCLUSION

54. We agree that it is appropriate for us to issue a declaratory ruling on whether the Maritime Satellite Act legally prohibits COMSAT from participating in Inmarsat-P. We express no opinion at this time on whether the Inmarsat Convention prohibits Inmarsat itself from participating in Inmarsat-P. We also do not address the other issues raised by Motorola.

55. We adhere to the interpretation of the Maritime Satellite Act set forth in *Aeronautical Services Order II*. Specifically, we hold once again that the Act prohibits COMSAT from offering non-maritime services through Inmarsat except to the extent that such services are "ancillary to and supportive of" COMSAT's provision of maritime services through Inmarsat.

56. Based on the record before us at this time, we conclude that the Inmarsat-P service which COMSAT intends to provide through an Inmarsat Affiliate cannot be considered "ancillary to and supportive of" COMSAT's provision of maritime services through Inmarsat. Even accepting COMSAT's arguments about the need to update Inmarsat's traditional maritime services, any service provided through the proposed Affiliate would be

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Comments of Ellipsat Corp. (July 12, 1994); Reply Comments of IDB Mobile Communications, Inc. (July 1, 1994). While some of the proposed conditions (such as the extent to which the Affiliate "succeeds to" Inmarsat's orbital assignments and spectrum allocations) might well be relevant to the test we set forth in the text, others (such as a requirement that all the Affiliate's governmental investors offer market access to the Affiliate's competitors) are clearly policy proposals which, despite their attractiveness on policy grounds, have little bearing on whether the proposed Affiliate would effectively extend COMSAT's statutory right of exclusivity.

just one more competitor, not an updated version of Inmarsat service. In addition, Inmarsat-P will require a capital investment in excess of all Inmarsat's capital investments to date, and is projected to lead to a dramatic increase in subscribers, the large majority of whom will be non-maritime subscribers. Furthermore, Inmarsat-P will use separate spectrum, satellites, and ground facilities, and will be operationally independent of Inmarsat's maritime services. These facts prevent us from finding Inmarsat-P "ancillary" to Inmarsat's maritime services in any reasonable sense of the word. Moreover, even if Inmarsat itself intended to provide Inmarsat-P services, the non-maritime aspects of the project could not be deemed ancillary to the maritime aspects.

57. We do, however, leave open the possibility that the Inmarsat Affiliate may be structured in such a way as to qualify as a "non-Inmarsat" line of business within the sense we intended in our *COMSAT Study*. In that circumstance, COMSAT's participation in Inmarsat-P would be permitted under the Maritime Satellite Act as long as it were "not inconsistent" with COMSAT's affirmative maritime obligations under that Act. In order to qualify as a "non-Inmarsat" business, the Affiliate would have to be structured in such a way that it did not in any way extend COMSAT's exclusive dealing arrangement with Inmarsat.

58. Accordingly, IT IS ORDERED that Motorola's petition be DENIED IN PART AND GRANTED IN PART, in accordance with this Memorandum Opinion and Order.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of the Application of	)	
	)	
THE SOUTHERN NEW ENGLAND TELEPHONE COMPANY	)	File No. W-P-C-6858
	)	
For Authority pursuant to Section 214 of the Communications Act of 1934, as amended, to construct, operate, own, and maintain facilities to test a new technology for use in providing video dialtone service in specific areas in Connecticut.	)	

ORDER AND AUTHORIZATION

Adopted: November 18, 1994 Released: November 22, 1994

By the Commission: Commissioner Barrett issuing a statement.

I. INTRODUCTION

1. Before the Commission is the request of The Southern New England Telephone Company ("SNET") to extend and amend its existing Section 214 authorization to provide video dialtone services on a trial basis.[1] SNET asks the Commission for authorization to expand its market trial to provide video dialtone services in two geographic areas for a period of one year. FiberVision Corporation ("FiberVision"), the National Cable Television Association ("NCTA"), and the New England Cable Television Association, Inc. ("NECTA") have filed pleadings against SNET's request.[2] SNET has filed a reply.

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1 See The Southern New England Telephone Co., 9 FCC Rcd 1019 (1993) (SNET Trial Order). SNET states its request "seeks to amend the terms of the authority previously granted in this proceeding in order to conduct an expanded market trial of a new technology to provide video dialtone service." SNET Transmittal Letter to William F. Caton, Acting Secretary, FCC (Dec. 15, 1993). SNET filed its Request for Extension and Amendment to Authorization on December 15, 1993.

2 FiberVision filed a Petition to Limit Request for Extension ("FiberVision Petition") on January 21, 1994. NCTA filed a Petition to Deny ("NCTA Petition") on January 24, 1994. NECTA filed comments on January 21, 1994.

2. For the reasons set forth below, we grant the request of SNET, subject to certain conditions and requirements that are designed to protect the interests of telephone ratepayers, video dialtone subscribers, and video programmer-customers.

II. BACKGROUND

3. In the VDT Order,[3] the Commission determined that video dialtone[4] would enable local telephone companies to participate in the video marketplace, without violating the statutory telephone company-cable television cross-ownership restrictions.[5] The Commission also determined that carriers must file a Section 214

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3 Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54-63.58, 7 FCC Rcd 5781 (1992) (VDT Order), aff'd & modified on recon., FCC 94-269 (Nov. 7, 1994) (VDT Recon Order), appeals pending sub nom. Mankato Citizens Tel. Co., et al. v. FCC, No. 92-1404, et al. (D.C. Cir. Sept. 9, 1992).

4 In the VDT Order, we defined "video dialtone" as the provision of a basic common carrier platform to multiple video programmers on a non-discriminatory basis. A "basic platform" is a common carriage transmission service coupled with the means by which customers (end users) can gain access to any or all video programming carried on that platform. If a local telephone company provides such a basic platform, it may also provide enhanced and non-common carrier services related to the provision of video programming in addition to basic common carrier services. 7 FCC Rcd at 5783, para. 2.

5 In August, 1993, the U.S. District Court for the Eastern District of Virginia declared the statutory telephone company-cable television cross-ownership restriction, codified at 47 U.S.C. § 533(b), unconstitutional because the restriction violates the First Amendment. Chesapeake & Potomac Tel. Co. v. United States, 830 F. Supp. 909 (E.D. Va. 1993). This decision applies only to Bell Atlantic and its subsidiaries. Three other federal district courts have also found the statutory cross-ownership restriction unconstitutional. See U S WEST, Inc. v. United States, No. C93-1523R (W.D. Wash. June 15, 1994); BellSouth Corp. v. United States, No. CV 93-B-2661-S (N.D. Ala. Sept. 23, 1994); Ameritech Corp. v. United States, No. 93 C 6642 (N.D. Ill. Oct. 27, 1994). SNET has filed a similar challenge in the district court for Connecticut. The Southern New England Tel. Co. v. United States, No. 394CV00080 (AVC) (D. Conn. filed Jan. 19, 1994).

application before constructing video dialtone facilities.[6]

4. On November 12, 1993, the Commission released an Order and Authorization granting in part SNET's application filed pursuant to Section 214 of the Communications Act of 1934, as amended,[7] and Sections 63.01 and 63.54 of the Commission's rules,[8] as amended by the Commission's VDT Order. The Order and Authorization approved SNET's proposal to conduct a technology and market trial for one year in its West Hartford, Connecticut telephone service area, subject to certain conditions.

5. In its initial application to provide video dialtone on a trial basis, SNET proposed to serve 1,600 subscribers through a hybrid fiber optic-coaxial cable distribution network. In this request, SNET seeks permission to expand the existing authority to allow construction of hybrid fiber-coax networks in two additional areas for a one year market and technical trial.[9] SNET proposes to construct facilities that would pass a total of 150,000 homes located in two geographic areas.[10] SNET anticipates a penetration rate of 12 to 13 percent or approximately 20,000 subscribers for the two areas combined.[11] SNET states that it will initially transport only video signals over its network.[12] The expanded trial would employ digital facilities able to offer 200 digital channels

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6 VDT Order at 5820, para. 72. Generally, Section 214 requires Commission authorization before a carrier extends a new line of interstate communication. For Section 214 purposes, a "line" means "any channel of communication established by appropriate equipment, other than a channel of communication established by the interconnection of two or more existing channels." 47 U.S.C. § 214(a).

7 47 U.S.C. § 214.

8 47 C.F.R. §§ 63.01, 63.54.

9 SNET Request for Extension and Amendment to Authorization ("SNET Request") at 2. One area SNET proposes to serve is the northern Connecticut towns of West Hartford (excluding the previously approved area), New Britain, Farmington, and Hartford. The second area SNET seeks authority to serve is comprised of Stamford, Norwalk, Darien, Westport, and Fairfield. Id. at i.

10 Id. at 2.

11 Id.; SNET Ex Parte Letter at (May 18, 1994) ("SNET Ex Parte Letter") at 5.

12 SNET Request at 4 n.5.

of video programming as well as transport to multiple, unaffiliated programmer-customers.[13] According to SNET, approximately 80 analog broadcast signals will also be delivered over the network.[14] In addition to a basic platform, SNET indicates that non-regulated video gateways could be offered that would permit subscribers to select the programming of their choice.[15] The expanded trial, if authorized, would also test enhanced and non-common carrier services.[16]

6. SNET contends that it needs a market trial of this size to ascertain the extent to which potential video dialtone subscribers will attract programmer-customers, and the extent to which programmer-customers will participate in order to attract subscribers to video dialtone service.[17] SNET plans to monitor and evaluate programmer-customer and subscriber price elasticities that it will use to determine future pricing structures and marketing strategies. The technology trial, SNET claims, will enable it to gain experience with new video dialtone technologies, with the delivery of services across large noncontiguous geographic areas, and in day-to-day operations of an advanced network.[18]

III. DISCUSSION

A. Proposed Expansion of Market and Technical Trial

Contentions of the Parties

7. FiberVision,[19] NCTA, and NECTA argue that SNET's request is

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13 Id. at ii, 4; SNET Ex Parte Letter at 1. SNET asserts that the network's large digital channel capacity ensures channel capacity adequate to serve multiple video programmers on a nondiscriminatory basis. Id.

14 SNET Request at 7; SNET Ex Parte Letter at 1.

15 SNET Request at 5.

16 Id.

17 Id. at 3.

18 Id. at 4-5. From an operational standpoint, SNET expects the expanded trial, which is "realistically-scaled," will help it to determine the costs of servicing and administering the video dialtone network and customer databases. Id.

19 FiberVision is a cable television operator that has applied for cable television franchises in four Connecticut franchise areas: Hartford, New Britain, New Haven, and Bridgeport.

for commercial video dialtone service, not an expansion of its previously authorized market and technical trial. FiberVision argues that the size of SNET's proposed trial is substantially larger than that of previous video dialtone trials.[20] FiberVision contests the size of SNET's proposed trial as unwarranted and SNET's projected penetration rate of 12 percent as disingenuous.[21] FiberVision contends that SNET has portrayed this request as an expanded trial to avoid giving specific information about its plans because the Commission requires more detail in applications to provide full commercial service than to conduct a trial.[22] Finally, FiberVision argues that SNET has failed to offer any adequate justification for a trial of this magnitude.[23]

8. NCTA states that it did not oppose SNET's original application because it appeared to be a bona fide one year technical trial limited to 1,600 homes.[24] SNET's instant proposal, according to NCTA, is not a true trial because SNET seeks to pass 150,000 homes, which is more than 10 percent of its telephone subscriber base.[25] NCTA contends that SNET has not shown that this sample is necessary to determine market demand for its proposed service, or that relevant market data are not already available from other sources.[26] Furthermore, NCTA and NECTA argue that SNET has no basis for requesting an expanded trial in light of its recent announcement to invest $4.5 billion to construct a fiber-coaxial broadband network throughout Connecticut that in addition to providing telephone service would be able to transport video

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FiberVision Petition at 4.

20 Id. at 12. FiberVision states that prior Section 214 authorizations for video dialtone trials ranged in size from three apartment buildings to 60,000 homes. Id. at 13, citing New York Tel. Co., 8 FCC Rcd 4325, 4330 para. 26 (1993); U S WEST Communications, Inc., 9 FCC Rcd 184, 188 n.57 (1993) (60,000 homes passed).

21 FiberVision Petition at 12.

22 FiberVision Petition at 13, citing New York Tel. Co., 8 FCC Rcd at 4330, para. 26.

23 FiberVision Petition at 30.

24 NCTA Petition at 2.

25 Id.

26 Id. See also NCTA Reply Comments (filed Feb. 25, 1994) at 4.

signals.[27] NCTA contends that, since SNET has already decided to make this multi-billion dollar commitment, there is no justification for allowing a trial, the purpose of which is to enable SNET to decide whether to proceed to a commercial video dialtone offering.

9. NECTA argues that, based on the sheer size of the proposed service areas, SNET's request cannot be considered a trial.[28] NECTA states that SNET proposes to "spend more money, pass more homes, and provide video dialtone service to a greater number of subscribers than New Jersey Bell in its proposal to offer actual [commercial] video dialtone service."[29] NECTA further contends that the Commission must consider the magnitude of the proposed SNET service in light of SNET's relatively small size.[30] NECTA argues that the initial cost of the proposed SNET trial is more than 50 percent greater than the cost of U S WEST's trial, and, while U S WEST and its shareholders may be able to absorb losses associated with the failure of its video dialtone trial, SNET is a smaller

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27 NCTA Petition at 2, citing George Judson, "Data Highway Accelerates in Connecticut," The New York Times, Jan. 13, 1994, at B1; NECTA Comments at 6, citing SNET News Release, Jan. 13, 1994 at 2. NECTA claims that SNET's construction plans are also motivated by a decision of the Connecticut Department of Public Utility Control permitting SNET to invest $400 million over four years to upgrade its network. NECTA Comments at 7, citing DPUC Review of Telecommunications Policies: Infrastructure Modernization, Competition, Pricing Principles and Methods of Regulation, Docket No. 91-10-06, at 41 (July 7, 1993).

28 NECTA Comments at 4. NECTA states that SNET's proposal "dwarfs the trials previously approved by the Commission." Id. NECTA points out that the SNET trial, if authorized, would be more than two and a half times larger in terms of homes passed than the largest approved trial of U S WEST. Id. at 4-5.

29 Id., citing Application, New Jersey Bell Tel. Co., File No. W-P-C-6838, filed Nov. 16, 1992. NECTA states that SNET fails to justify why it must serve the entire proposed service area to obtain "verifiable market data," arguing that the "Section Two Territory" is homogenous. Id. at 9. NECTA states that Westport and Fairfield are almost entirely residential, with a significant portion of their residents highly educated, wealthy, and predominantly white. Id. n.27, citing Bureau of the Census, U.S. Dep't of Commerce, 1990 Census of Population and Housing Summary Tape File 3A (040-Connecticut).

30 NECTA Comments at 6.

company and its proposed trial is "significantly" larger.[31] According to NECTA, a loss of SNET's $52 million investment in its video dialtone undertaking would represent a loss of more than 40 percent of SNET's net income.[32]

10. In response, SNET maintains that its request is for a trial and should be evaluated as such. SNET asserts that, notwithstanding contentions of NCTA and NECTA to the contrary, the size of a proposed trial or the number of homes passed does not determine whether a proposed offering is a trial or a permanent commercial service.[33] Rather, SNET argues that its request satisfies the two criteria required to obtain Commission authorization of a video dialtone trial. First, SNET states that its proposal is limited to one year and is to occur in a limited geographic area.[34] Second, SNET contends that it has demonstrated a need for, and a plan to obtain, data necessary to develop a permanent commercial offering.[35] SNET claims, through the statement of a marketing trial expert, that a subscriber base of 20,000 homes is necessary to obtain reliable marketing data from an area of varying population density and different demographics.[36] SNET disputes FiberVision's claim that SNET can provide service to 20,000 subscribers with a smaller network. SNET maintains that a 12 to 13 percent penetration rate is reasonable for a one-year trial of the size proposed.[37] Furthermore, in response to the argument that SNET's penetration estimate is unfounded, SNET contends that (1) its estimate is consistent with U S WEST's estimate for its video dialtone trial in Omaha, Nebraska, which has

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31 Id. at 5, 6. NECTA states that, compared to U S WEST's $954 million in net income on net assets of $19 billion, SNET's assets are less than $3 billion, producing net income of approximately $128 million in 1991. Id. n.15.

32 Id. at 6.

33 SNET Reply to Oppositions to Application for Extension of VDT Trial at 5 (Feb. 14, 1994) ("SNET Reply").

34 Id. at 6.

35 Id.

36 Id. at 7; Exh. 1. SNET contends that programmer-customers prefer a trial because it allows them to test various video programming alternatives with end users. SNET Ex Parte Letter at 6.

37 SNET Reply at 7; SNET Ex Parte Letter at 4. SNET argues that its penetration rate is consistent with the 15 percent penetration rate proposed by U S WEST in its approved trial.

been approved by the Commission, and (2) it is reasonable to expect a higher subscription rate for the West Hartford trial because service in the West Hartford trial will be free of charge while service in the expanded trial area will be available only for a fee.[38]

11. SNET states that NCTA's and NECTA's claims that the application should be evaluated as a permanent commercial offering solely because the proposed trial will use parts of SNET's new advanced broadband network are "baffling."[39] SNET argues that subscribers would be required to pay unnecessarily high prices if SNET were required to construct a stand-alone video dialtone network when a single network could provide both narrowband and broadband services, including video dialtone.[40]

Discussion

12. We conclude that SNET's application is a bona fide proposal for a video dialtone trial. We have repeatedly declined to set fixed standards regarding the size and duration of video dialtone proposals to determine whether they constitute trials or commercial offerings, and we do so again here.[41] We continue to believe that a "case-by-case review of video dialtone proposals better serves the public interest and will allow video dialtone to develop according to market forces."[42] We find that, under the circumstances, the proposed size of SNET's expanded trial is reasonable.[43] SNET has demonstrated through expert testimony that

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38 SNET Reply at 7-8, citing U S WEST Communications, Inc., 9 FCC Rcd at 185, para. 5 n.11, 186, para. 13 n.31. SNET also explains that, because of the larger size of the expanded trial, it will use less efficient marketing techniques (such as direct mail) rather than door-to-door marketing used in the West Hartford trial. SNET Reply at 8.

39 SNET Reply at 8.

40 Id. SNET argues that it would be "irrational" to classify video dialtone service as either trial or commercial service based on the type of network employed to provide transport. Id.

41 See, e.g., U S WEST Communications, Inc., 9 FCC Rcd at 188, para. 22.

42 Id.

43 See infra para. 55 (finding that, even in light of 29 percent penetration rate achieved in West Hartford video dialtone trial, the penetration estimate for the expanded trial is not

an expanded trial of this size is reasonably calculated to lead to valuable marketing, technical, and operational data. SNET's marketing expert avers that, for SNET successfully to evaluate potential marketplace demand for video dialtone in a relatively short time frame, "it is both prudent and imperative that a large scale test be created."[44] According to Dr. Steven Permut, SNET's marketing expert, it is reasonable and appropriate "to create a trial situation of such expanded size and scope . . . in order to simultaneously evaluate a number of potentially relevant variables with a level of statistical confidence that would realistically guide management's future investment and deployment decisions."[45] Petitioners simply rely on arguments that SNET's proposed trial size is unprecedented and fail to address Dr. Permut's testimony regarding the proposed size relative to the limited duration of this market trial.

13. Significantly, we note that the expanded trial is limited in duration and in scope, and furthermore, we herein impose certain conditions on SNET's authorization that are intended, inter alia, to protect telephone ratepayers and trial participants. To this end, we will require SNET to inform participants in the expanded trial, including both programmer-customers and video dialtone service subscribers, that SNET is conducting a trial of video dialtone services, that the trial is limited to one year, and that SNET may or may not seek Commission approval to offer video dialtone on a commercial basis after the trial ends. We have imposed a similar obligation on carriers conducting market trials of enhanced services.[46] The purpose of the notification requirement is to ensure that programmer-customers and end-user subscribers understand that the services offered during the trial are approved for a specified period of time and may not be available on an on-going basis after the trial.[47]

14. In the VDT Order, we declined to specify the technology, network architecture, or functions that a telephone company could

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an unreasonable estimate).

44 SNET Reply, Exhibit 1, para. 5.

45 Id., para. 10.

46 See BOC Notices of Compliance with CEI Waiver Requirements for Market Trials of Enhanced Services, 4 FCC Rcd 1266, 1269, 1272 (1989).

47 See id. at 1269, para. 28.

offer under video dialtone.[48] Our video dialtone policy "relies upon the technical and market creativity of those in the private sector responding to market demand and economics to determine the substance of telephone company video dialtone offerings."[49] In permitting SNET to conduct a relatively large expanded market and technical trial, we are guided by these principles of regulatory and business flexibility that can, in turn, foster economic opportunity. Without first conducting either a technical or market trial, smaller telephone companies, like SNET, may be reluctant to invest significant capital in a commercial offering of video dialtone.[50]

15. The petitioners and commenters have presented no persuasive basis to deny or otherwise limit the SNET expanded trial. We do not find persuasive arguments that the application should be denied simply because SNET proposes to pass more homes than any other prior trial application. SNET has demonstrated, through expert testimony, that in comparison with a more limited trial a trial of this size conducted in two different geographic areas can lead to more useful marketing data that can be used by SNET and its programmer-customers.[51] As discussed above, SNET has presented evidence that a market trial of this size is reasonable and necessary to evaluate potential demand for video dialtone services in a relatively short time period.[52] Moreover, according to SNET, the size of its sample will enable it to obtain statistically valid conclusions based on a variety of demographic, income/employment, life style, and behavioral variables.[53]

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48 VDT Order at 5788, 5805, paras. 13, 45 ("The record makes clear that the specific services that will be offered or network architectures that will be deployed are not yet certain at this time and thus, regulatory flexibility is key if video dialtone is to develop in accordance with market needs and technological innovations rather than according to Commission mandate"); see VDT Recon Order at 17, para. 34.

49 Id.

50 See U S WEST Communications, Inc., 9 FCC Rcd at 186, para. 13 ("U S West states that although it plans to deploy a video dialtone service if the Omaha trial is successful, it is unwilling to introduce a general video dialtone service until it has tested both the technology and market for video dialtone service" (footnote omitted)).

51 See SNET Reply, Exhibit 1, paras. 5, 8, 10, 17.

52 See supra para. 12.

53 SNET Reply at 6.

Conducting the trial in two different parts of the state will also enable SNET to compare data from socio-economically diverse areas. SNET states that the median household income in parts of the Hartford area is significantly below the state average while the median household income for the Westport-Darien area is significantly above the state average.[54] In addition, SNET proposes to serve both New Britain and Farmington, where white collar employment is 26 percent and 44 percent respectively, compared to a statewide average of 33 percent.[55] The application's opponents do not directly address the issue of effective market trial size and the statements made by SNET's market trial expert.

16. NECTA raises concerns about the effect of the expanded trial on SNET ratepayers if after the trial SNET decides not to deploy commercial video dialtone service. NECTA contends that this application is different from previous trials that the Commission has approved because SNET is a relatively small telephone company and the costs of the trial are estimated at $52.6 million or approximately 40 percent of SNET's annual net income.[56] On the other hand, NECTA also argues that the proposed VDT trial is actually the initial stage of SNET's $4.5 billion rebuild of its telephone network infrastructure.[57] Indeed, SNET states that the video dialtone trials are part of its modernization plan and that the initial deployment will be of hybrid fiber-coaxial facilities that can be used in providing both broadband and narrowband services.[58] SNET has clarified that the $52.6 million figure cited in its application includes both shared facilities and facilities that will initially be used for providing video service.[59] SNET will not provide telephony over those latter facilities, however, until it obtains Commission approval of a plan for separating the costs of the shared facilities.[60]

17. We do not find the estimated cost of the expanded trial to justify denial of the application. In the event the expanded trial is not successful, SNET will assign all costs associated with

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54 Id. at 7.

55 Id., citing Claritas computer database (based on U.S. Census data).

56 NECTA Comments at 6.

57 NECTA Reply Comments at 6.

58 SNET Reply at 3-4.

59 SNET Ex Parte Letter at 4-5.

60 SNET Reply at iv, 9.

those parts of the upgraded network that are not useful in the provision of regulated telephone services to its corporate stockholders.[61] In addition, SNET agrees to obtain Commission approval for any cost allocation plan before using the facilities for regulated telephone service. Those commitments from SNET will be made conditions of our approval of the trial. We believe that these safeguards will adequately protect SNET's ratepayers from paying for any loss that may occur from the trial.

B. VDT Order Issues

18. For local telephone companies to offer video dialtone service, they must make available a basic common carrier platform to multiple video programmers on a nondiscriminatory basis, and a "means by which customers can access any and all of the video programming" offered.[62] The platform must provide "sufficient capacity to serve multiple video programmers."[63]

Contentions of the Parties

19. According to FiberVision, SNET's application to expand its market and technical trial contains less information than its initial West Hartford application.[64] FiberVision contends that SNET's request fails to show that its system will provide nondiscriminatory access for multiple programmers.[65] Moreover, FiberVision states that SNET does not provide information about who will be the programmer-customers.[66] FiberVision also questions the relationship between SNET and CAI Wireless Systems, Inc. (CAI), a wireless cable operator who has been providing video programming for the West Hartford trial and has committed to providing programming for the expanded trial.[67] FiberVision claims that SNET also fails to provide a cost allocation methodology and rates to be

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61 Id. at 14-15 n.23.

62 VDT Order at 5783, para. 2 & n.3.

63 Id. at 5797, para. 29.

64 FiberVision Petition at 15.

65 Id. at 14.

66 Id.

67 FiberVision's Motion for Leave to File Supplemental Factual Material (Feb. 17, 1994) at 2. FiberVision's motion to supplement the record is granted.

charged for service.[68] FiberVision maintains that SNET's application does not adequately describe the technical specifications of its system and asserts that SNET's proposal relies on digital technology that is not yet commercially available.[69]

20. NCTA argues that, before the Commission approves SNET's application, it should adopt and implement regulatory safeguards for video dialtone service.[70] NCTA claims that the Commission needs to address issues of jurisdictional separation, cost accounting, access charges and price caps, regulated and non-regulated service cost separation, joint marketing, and customer privacy.[71] In its reply comments, NCTA maintains that SNET has failed to provide sufficient information for the Commission reasonably to evaluate its application.[72] NCTA also states that SNET does not provide figures on common costs.[73]

21. Similarly, NECTA maintains that SNET has failed to provide adequate information for the Commission to evaluate its proposed service and that the Commission must demand additional information before assessing the application.[74] NECTA states that SNET fails to provide sufficient cost accounting data and to describe its cost accounting methodology.[75] NECTA contends that the application does not adequately describe the proposed video dialtone service. NECTA asserts that, based on the quality of the information provided in the application, there is no way to determine if the application complies with the requirements of the

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68 FiberVision Petition at 14.

69 Id. at 15.

70 NCTA Petition at 3; NCTA Reply Comments at 5-6.

71 NCTA Petition at 4-6.

72 NCTA Reply Comments at 7. The level of specificity currently provided by SNET in the application, NCTA argues, does not permit the Commission to assess the reasonableness of investment expenditures or to determine whether the proposal is economically justified. Id. NCTA suggests that the Commission require SNET to submit an economic justification statement. Id.

73 Id. at 6.

74 NECTA Comments at 11; NECTA Reply Comments at 9.

75 NECTA Comments at 11-12; NECTA Reply Comments at 10, 12-15.

VDT Order.[76] NECTA argues that SNET has not demonstrated that its proposed basic service will be available to multiple video programmers.[77] NECTA adds that the application fails to provide a description of SNET's proposed gateway service.[78]

22. SNET responds that requests for additional information are unfounded and are intended to delay the Commission's grant of authorization.[79] SNET states that it will assign to the trial all costs associated with the construction and operation of the network "because SNET does not contemplate using the network to provide any other regulated service during the proposed one-year VDT [video dialtone] trial."[80] SNET avers that, before any video dialtone costs are assigned to the regulated rate base, it will obtain Commission approval and will comply with Parts 32 and 64 of the Rules.[81] Furthermore, SNET asserts that it will only use an "insignificant" amount of its existing telephone plant to provide video dialtone service, and that it "will directly assign the costs of this plant to the VDT [video dialtone] trial."[82] SNET claims that, contrary to petitioners' assertions, the proposed service will offer nondiscriminatory access to programmers and will have sufficient capacity to accommodate multiple programmers.[83] SNET contends that it will have no capacity problems because it "expects to increase channel capacity to at least 300 channels shortly after the expanded trial begins through digital compression."[84] With regard to channel allocation, SNET indicates that a video programming packager has requested 40 analog channels to offer a

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76 NECTA Comments at 17.

77 Id.; NECTA Reply Comments at 16. NECTA states that SNET also fails to describe a channel allocation scheme. NECTA Comments at 17. Without a description of an access method, NECTA claims that there is no way to determine whether there will be sufficient capacity on the system to accommodate multiple customer-programmers. NECTA Reply Comments at 16.

78 NECTA Comments at 17; NECTA Reply Comments at 11.

79 SNET Reply at 13.

80 Id. at 14, citing SNET Request for Extension and Amendment to Authorization at 7, 11.

81 SNET Reply at 14; SNET Ex Parte Letter at 4.

82 Id.

83 Id. at 17-18.

84 Id. at 18.

"cable-like" programming package to end user subscribers.[85] SNET also states that a local television affiliate and a community college have requested dedicated analog channels to provide video programming.[86]

Discussion

23. The video dialtone regulatory framework requires, as a prerequisite to a local telephone company's provision of video dialtone service, the establishment of a basic common carrier platform containing sufficient capacity to serve multiple video programmers.[87] The basic common carrier platform must give multiple video programmers nondiscriminatory access to a common carrier transmission service that will enable them to deliver, and consumers to receive, video programming and other information services.[88] In addition, the system's capacity must be able to expand to accommodate increasing demand so as not to become a "bottleneck."[89] In the SNET Trial Order, we stated that, in determining whether the application satisfied the capacity requirement, we would review each application on a case-by-case basis taking into consideration: (1) the initial capacity available; (2) the ability to expand this capacity; (3) the demand for capacity; and (4) the proposed duration of the offering for applications to provide video dialtone on a trial basis.[90]

24. We find that SNET will be providing a common carrier platform with sufficient capacity to serve multiple video programmers that satisfies the requirements of the VDT Order. The initial capacity of SNET's system will include 80 analog channels

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85 SNET Ex Parte Letter at 1.

86 Id.

87 47 C.F.R. § 63.54(d)(2); VDT Order at 5797, para. 29.

88 47 C.F.R. § 63.54(d)(2); VDT Order at 5797, para. 29. We determined in the VDT Order that pursuant to Section 201(a) of the Act, 47 U.S.C. § 201(a), a local telephone company offering a video dialtone platform must furnish capacity to video programmers upon reasonable request, and that pursuant to Section 202(a), 47 U.S.C. § 202(a), such capacity must be provided without unreasonable discrimination. VDT Order at 5798 n.69.

89 VDT Order at 5783, para. 2, 5797, paras. 29-30.

90 SNET Trial Order at 1022 n.46.

and 200 digital channels.[91] SNET will be required to expand the system's capacity to the extent that expansion is technically feasible and economically reasonable in the context of its trial.[92] SNET will be required to notify the Chief of the Common Carrier Bureau of any anticipated or existing capacity shortfall and of plans for addressing such shortfall.[93] Such notice must be provided within thirty days of the date SNET becomes aware of an anticipated capacity shortfall or within five days after denying a video programmer access to the video dialtone platform because of capacity limitations, whichever occurs first. To the extent SNET concludes that expansion of its platform during the trial is not technically feasible or economically reasonable, it must, at that time, explain in detail the basis for its determination.

25. Based on the record in this proceeding, we find the proposed capacity of the video dialtone platform to be sufficient. In connection with demand for channel capacity, SNET states that from its discussions with video information providers few programmers want dedicated channels.[94] Rather, "[m]ost have a desire to obtain access to individual time slots and the Video-On-Demand (VOD) capabilities of the platform."[95] SNET indicates that it has commitments from 22 video programmers to provide programming on the expanded trial platform.[96]

26. Thus we find that SNET has satisfied the video dialtone capacity requirement. We conclude that the availability of 80 analog channels, and eventually 200 digital channels in mid-1995, should initially be adequate to serve multiple video programmers. Demand for capacity appears to exist and SNET assures us that it will take reasonable steps to meet any additional requests for capacity on the platform.[97] Finally, we note that the expanded trial will be limited to one year.

27. Consistent with our Order and Authorization granting SNET

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91 SNET Request at ii, 8; SNET Reply at 15, n.25, 16; SNET Ex Parte Letter at 1.

92 See VDT Recon Order at 18, para. 38.

93 Id.

94 SNET Ex Parte Letter at 1.

95 Id.

96 SNET Reply, Exh. 5.

97 See SNET Trial Order at 1020, para. 6; SNET Ex Parte Letter at 3.

permission to conduct a technology and market trial in West Hartford, we find that SNET has committed to providing video programmers nondiscriminatory access to the basic platform.[98] According to SNET, the system's channel capacity will ensure that multiple video programmers can gain nondiscriminatory access to the platform.[99] SNET's initial application provided that each programmer-customer will be able to offer multichannel and single channel broadcast service as well as on-demand video services to end users.[100] SNET also stated that the terms and conditions for access to the platform will be governed by tariff.

28. In the VDT Order, we stated that local telephone companies may not determine how video programming is presented for sale to consumers, including making decisions concerning bundling, tiering, or the price, terms, or conditions of video programming to consumers.[101] We conclude that SNET will not be impermissibly involved in the offering or presentation of video programming directly to subscribers. According to SNET, programmer-customers will be solely responsible for the selection, charging, and control of video programming provided to subscribers.[102] In addition, SNET states that marketing and promotional materials, including programming guides, will clearly indicate that each programmer-customer is responsible for the video programming and that SNET is not responsible for the selection of any video programming.[103] In its video dialtone application, SNET has not proposed to use the platform to provide, either directly or indirectly through an affiliate, video programming to its subscribers during the trial.[104] Telephone company provision of video programming (if otherwise lawful) raises a host of regulatory issues not addressed in any detail in this record that would need to be decided prior to permitting such activity. Allowing SNET to provide video programming in advance of resolving these issues would not serve the public interest. We therefore conclude that the public convenience and necessity requires, at this time, a condition on

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98 SNET Trial Order at 1022, para. 15.

99 SNET Request at 4.

100 SNET does not indicate that its plans have changed for the expanded trial.

101 VDT Order at 5789, 5817, paras. 14, 69.

102 SNET Initial Application at 7; SNET Request at 11; SNET Ex Parte Letter at 1, 2.

103 SNET Ex Parte Letter at 3.

104 See Request at 11.

this authorization that SNET not, either directly or indirectly through an affiliate, provide video programming directly to subscribers on this video dialtone system without further action by the Commission. Finally, we also find that FiberVision's argument that a SNET officer may be impermissibly associated with one of SNET's programmer-customers is moot because SNET states that the official will not be joining the programmer's board of directors.[105]

29. We require SNET to account for all costs associated with the expanded trial, including development costs and expenses, in accordance with Part 32.[106] To ensure that these costs are not borne by ratepayers of other regulated services, we require SNET to segregate all costs incurred in providing video dialtone service into subsidiary accounting records and to assign these costs to the video dialtone trial. If these costs are not recovered from future video dialtone services, they must be borne by shareholders rather than the ratepayers of other regulated services.[107] In addition, accurate copies of the subsidiary accounting records shall be submitted to the Commission on a quarterly basis. We delegate to the Chief, Common Carrier Bureau the authority to determine the content and format of the records as well as the quarterly reports. We note that these requirements are wholly consistent with the approach taken in other video dialtone trial authorizations.[108] In the event that SNET wishes to offer local exchange and exchange access telephone services over the upgraded network during the trial, it must first submit and obtain approval of an accounting and cost allocation plan that is consistent with our then-existing rules.[109]

30. We also require SNET to account for the cost of non-common carrier and enhanced services or video customer premises equipment (CPE) in accordance with our rules, to the extent SNET

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105 Letter from Counsel for SNET to Chief, Domestic Facilities Division, FCC (March 3, 1994) at 2.

106 See SNET Request at 10-11.

107 See, e.g., The Chesapeake & Potomac Tel. Co. of Virginia, 8 FCC Rcd at 2316, para. 13; New York Tel. Co., 8 FCC Rcd at 4329, para. 23.

108 See, e.g., The Chesapeake & Potomac Tel. Co. of Virginia, 8 FCC Rcd 2313 (1993); New York Tel. Co., 8 FCC Rcd 4325 (1993); U S WEST Communications, Inc., 9 FCC Rcd 184 (1993).

109 See, e.g., U S WEST Communications, Inc., 9 FCC Rcd at 190, para. 31.

offers such services or equipment during the trial.[110] We conclude that SNET's proposed provision of these services and video CPE is consistent with the requirements contained in Section 63.54(d)(2) of our rules.[111] We require that, to the extent the non-regulated components of the expanded video dialtone trial are not already covered by SNET's cost allocation manual (CAM), SNET must revise its manual to show how it intends to allocate costs of such components between regulated and non-regulated activities for the duration of the trial.[112] Any necessary revisions must be filed within thirty days after release of this Order, and sixty days before providing non-regulated services related to video dialtone. At a minimum, in its submission, we require SNET to list all accounts affected by its provision of non-regulated services associated with its video dialtone trial, and also describe those services. All temporary CAM revisions related to the trial will be subject to public comment and Commission scrutiny. SNET must file permanent revisions if and when it decides, and is authorized, to offer commercial video dialtone services. We emphasize that our decision here, and the conditions we attach to it, are without prejudice to and in no way constrain any action that we may take in later phases of the video dialtone proceeding or any other applicable rulemaking proceeding.

C. Section 214 Issues

31. In the VDT Order, the Commission decided that applications to provide video dialtone must be filed pursuant to Section 214 of the Communications Act.[113] In order to authorize an application under Section 214, the Commission must determine that a grant would serve the "public convenience and necessity."[114]

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110 SNET has confirmed that all equipment located on the premises of video dialtone subscribers will be provided as CPE. SNET Request at 8, Exh. 3 at 2; see 47 C.F.R. § 64.702(e) (CPE is separate and distinct from common carrier communications services and must be provided on untariffed basis).

111 47 C.F.R. § 63.54(d)(2).

112 See 47 C.F.R. § 64.903(b) (CAM revisions must be filed with the Commission sixty days before non-regulated services are offered to subscribers).

113 VDT Order at 5820, para. 72. The Commission found that video dialtone applications must be filed pursuant to Section 214 because "the basic video dialtone platform is presumptively an interstate service over which the FCC has exclusive jurisdiction." Id.

114 47 U.S.C. § 214(c).

Traditionally, the focus of the Section 214 review has been "to ensure that carriers prudently invest in equipment so as to avoid waste and unreasonably high rates" for telephone rate payers.[115] The courts have granted the Commission significant latitude in making its determinations under Section 214.[116] In the VDT Order, the Commission concluded that our existing safeguards were sufficient to protect against potential discrimination and cross-subsidy by telephone companies offering video dialtone, but stated our intention to reassess their adequacy as Section 214 applications for specific video dialtone systems were filed.[117]

Contentions of the Parties

32. FiberVision contends that the SNET proposal will not serve the public interest because its proposed system is not technologically advanced or innovative, will stifle competition, and will not create consumer choice fairly or evenly. FiberVision asserts that, because SNET's proposed system "involves no technological advances beyond current cable construction practices,"[118] the system does not satisfy the Commission's goal of improving the nation's telecommunications infrastructure.[119] FiberVision also alleges that SNET's proposal will restrain competition. According to FiberVision, SNET plans to "cherry-pick" the most profitable portions of the Hartford franchise area, serving only the wealthiest and most densely populated residential neighborhoods, while FiberVision must by law serve all portions of

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115 AT&T Request for Authorization to Supplement Existing Lines, File No. W-P-C-5560 (released March 10, 1986).

116 See Century Federal, Inc. v. FCC, 846 F.2d 1479 (D.C. Cir. 1988); General Tel. Co. of the Southwest v. United States, 449 F.2d 846 (5th Cir. 1971). In General Telephone Company of the Southwest, the court noted that "'[t]he Commission is not required to make specific findings of tangible benefit. It is not required to grant authorizations only if there is a demonstration of facts indicating immediate benefit to the public. . . . [B]ut the Commission must at least warrant . . . that competition [resulting from the grant] would serve some beneficial purpose . . . .'" General Telephone Company of the Southwest, 449 F.2d at 858, citing FCC v. RCA Communications, Inc., 346 U.S. 86, 96-97 (1953).

117 VDT Order at 5827, para. 89.

118 FiberVision Petition at 18. FiberVision notes that SNET's proposed video dialtone network currently cannot be used for telephony. Id., citing SNET Request at 4, n.5.

119 Id., citing VDT Order at 5795, para. 25.

the franchise area.[120] Moreover, FiberVision asserts that, since the identities of SNET's programmer-customers are not known, it is impossible to ascertain whether the proposed test will expand consumer choices.[121]

33. NCTA and NECTA argue that SNET has failed to provide sufficient information for the Commission to determine reasonably if SNET's proposal is economically justified.[122] The petitioners claim that, based on current information provided by SNET, the proposal is not economically viable.[123] At a minimum, the petitioners argue that the Commission should require SNET to provide more detailed cost and financial information about its proposed system.[124]

34. In its reply, SNET argues that it will not have an unfair competitive advantage if its application is approved.[125] SNET disputes FiberVision's claim that cable operators are required to serve all geographic areas in their serving areas arguing that "government policy" gives cable operators broad discretion to select the areas they wish to serve.[126] SNET maintains that neither federal law nor state law dictates the geographic areas that cable operators in Connecticut must serve.[127] In response to FiberVision's

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120 FiberVision Petition at 21-22. FiberVision argues that Section 621(a)(3) of the Communications Act, 47 U.S.C. § 541(a)(3), and Section 16-331(a)(2) of Connecticut law require FiberVision, as a franchised cable operator, to offer service to all homes in a franchise area, including lower income and less dense areas, while SNET is free to serve whomever it wants giving it an unfair market advantage. Id. at 21-23.

121 Id. at 28.

122 NCTA Reply Comments at 7; NECTA Comments at 12; NECTA Reply Comments at 10.

123 NCTA Reply Comments at 7; NECTA Comments at 13, citing Declaration of Patricia D. Kravtin at 12-15 and Tables 1 and 2; NECTA Reply Comments at 10.

124 NCTA Reply Comments at 7; NECTA Comments at 13; NECTA Reply Comments at 10-11.

125 SNET Reply at 9.

126 Id. at 10.

127 Id. SNET notes that the federal statute cited by FiberVision requires that a cable operator make service available to all homes within the service area the operator has chosen to

contention that SNET's network design is not advanced telecommunications infrastructure, SNET states that the system is state-of-the-art and will offer the innovative services the Commission envisioned in the VDT Order.[128] SNET claims that its network will permit "video on demand" at the outset of operation in contrast to FiberVision's cable systems. SNET asserts that authorization of its trial will provide increased consumer choice and that FiberVision's claims to the contrary are incorrect.[129]

Discussion

35. We conclude that the public convenience and necessity will be served by granting Section 214 authority to SNET for the expansion of its video dialtone technical and market trial in the Stamford and Hartford, Connecticut service areas, subject to certain conditions.[130] The Commission has a mandate under the Communications Act to encourage technological innovation in communications and to expedite the introduction of new technology subject to other public interest considerations.[131] Indeed, the Commission's rules recognize that experiments can be useful to develop new technologies and evaluate their acceptability to users.[132] Significantly, in the VDT Order, the Commission found that it is in the public interest to encourage trials of video dialtone technology in order to fulfill our goals of promoting an advanced, cost-effective telecommunications infrastructure.[133]

36. FiberVision's contentions that SNET's technical proposal is not advanced are not persuasive. The hybrid fiber-coaxial architecture SNET has proposed to use for its expanded trial will provide sufficient bandwidth for the provision of voice, video, and data services. In addition, hybrid fiber-coax facilities could be

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serve. Id. The state regulation cited by FiberVision, according to SNET, "gives cable operators the right to seek to limit the communities they serve." Id.

128 Id. at 15.

129 Id. at 21.

130 See supra note 9, for the specific towns to be served by SNET in the expanded trial.

131 47 U.S.C. §§ 151, 157, 218.

132 See, e.g., 47 C.F.R. § 5.1 (experimental radio services).

133 VDT Order at 5836, para. 105.

used for advanced interactive and multimedia applications.[134] Currently, these services are not widely available on an integrated basis due to the existing technical limitations of twisted copper pair. The Commission has stated that the construction of advanced telecommunications facilities capable of transporting voice, video, and data services, like hybrid fiber-coax networks, is in the public interest.[135] SNET's West Hartford video dialtone pilot and its instant proposal are but one part of its extensive state-supported plans to modernize Connecticut's telecommunications infrastructure. In sum, we find that SNET's proposed test of a hybrid fiber-coax architecture advances the Commission's goals of establishing a technologically advanced, cost-effective national telecommunications infrastructure, promoting additional competition in the local video distribution market, and fostering a diversity of video services in order to create additional opportunities for consumer choice.

37. Trials are, by definition, tests of a controlled experimental nature which are typically limited in duration and in scope. We have previously concluded that "a trial [application], by definition, is not generally susceptible to the same level of precision" as an application for permanent video dialtone service.[136] As a matter of policy, the potential benefits that may be realized by conducting limited trials may outweigh perceived risks created by subjecting video dialtone trial applications to less scrutiny. In its request, SNET proposes to expand its existing trial of video dialtone services to two discrete geographic areas for a period of one year. SNET plans to conduct a market study and compare the expanded trial areas. Due to the experimental, limited nature of SNET's proposal, and the fact that SNET will be conducting a large scale market study of two distinct geographic areas, we find that it is in the public interest to subject this application to a less exacting level of scrutiny than that we would apply to an application for permanent, commercial video dialtone service.[137] We

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134 See SNET Request at 2.

135 VDT Order at 5795, para. 25.

136 New York Tel. Co., 8 FCC Rcd at 4330, para. 26; see U S WEST Communications, Inc., 9 FCC Rcd at 188, n.57.

137 See New York Tel. Co., 8 FCC Rcd at 4330, para. 26. Our action in no way limits our ability to ensure, in the subsequent tariff review process, that SNET's tariffed rates for video dialtone service during this market trial are just and reasonable. See VDT Recon Order at 101, para. 214. It is clear that consideration of costs in a Section 214 proceeding is distinct from the examination of rates in the tariff review process. All American Cables and Radio, Inc., File No. W-P-C

find that the potential public interest benefits of a limited, one-year trial of this size outweigh any possible risks, and furthermore, we believe this is consistent with Section 214 of the Act because it is part of our effort to encourage investment in an advanced telecommunications infrastructure.

38. Trials afford carriers the flexibility to decide how they will test their technology and marketing strategies. The Commission has repeatedly stated its intention not to influence the development of or endorse certain technologies or services in the video dialtone context.[138] We believe that it would be inappropriate for the Commission to interfere with carriers' decisions regarding trials of video dialtone technologies or services. At this time, video dialtone is in the early stages of deployment and testing -- the Commission has only authorized six carriers to offer video dialtone service. We believe that, through the trial process, carriers can be given a certain amount of flexibility to explore the commercial and technical viability of video dialtone.

39. Under these circumstances, we find that SNET has provided adequate economic justification for its video dialtone trial proposal.[139] SNET has provided estimated cost information in its application and states that the risks involved in this large scale trial will rest with its investors.[140] In the event the trial is unsuccessful and SNET decides to discontinue its video dialtone service, SNET states that the costs of video specific equipment and

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4990 (Com. Car. Bur. released May 7, 1986) at para. 5. As the Commission staff stated in a 1986 decision: "[a] detailed inquiry into tariff related matters . . . would vitiate the distinction between tariff and facilities authorization procedures and would require the Commission to engage in duplicative processes." AT&T Request for Authorization to Supplement Existing Lines, File No. W-P-C 5560 (released March 10, 1986) at para. 8.

138 VDT Order at 5793-94, 5797, 5804, paras. 22, 30, 44; Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54-63.58, 7 FCC Rcd 300, 310-11, para. 18 (1991); see supra para. 14 and n.49.

139 See Century Federal, Inc. v. FCC, 846 F.2d 1479, 1481 (D.C. Cir. 1988) (under circumstances of the case, court held that it was entirely within the Commission's discretion to accept a minimal showing of financial justification for new construction under Section 214).

140 SNET Ex Parte Letter at 6.

facilities will be borne by company shareholders.[141] Of course, should SNET file a Section 214 application to offer video dialtone service on a permanent, commercial basis, we expect it to fully comply with the application requirements set forth in our rules and adhere to the rules and policies established in the VDT Recon Order. With regard to claims that SNET proposes to serve only the wealthiest and most densely populated residential communities, we repeat our belief that a trial authorization affords SNET the flexibility to decide how and where its limited trial of video dialtone service will be offered. We reiterate our belief that a trial is intended to provide carriers flexibility to experiment and test new technologies and marketing strategies under "real world" conditions. However, several organizations have raised the issue of "electronic redlining" generally, and the Commission is currently carefully considering the issue in a separate proceeding.[142]

D. Motion for Investigation

Contentions of the Parties

40. On March 13, 1994, NECTA filed a motion for investigation with the Commission.[143] NECTA alleges that SNET may have violated Section 214 of the Act because SNET has commenced construction of facilities to be used for video dialtone service without prior Commission authorization.[144] NECTA asks the Commission to investigate SNET's construction activities, suspend consideration of SNET's pending request to expand its video dialtone trial, and, if the Commission finds that SNET has begun construction of video dialtone facilities without authorization, to take appropriate

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141 SNET Ex Parte Letter at 6; SNET Reply at 14 n.23; see SNET Trial Order at 1023, para. 18. In addition, we note that the rates in SNET's market trial tariff will be required to recover all the direct costs of the trial (including incremental costs plus a reasonable allocation of costs associated with shared plant), and a reasonable allocation of overhead costs. VDT Recon Order at 102, paras. 217-220.

142 Petition for Rulemaking to Adapt the Section 214 Process to the Construction of Video Dialtone Facilities and Petition for Relief of the Center for Media Education, Consumer Federation of America, Office of Communication of the United Church of Christ, National Association for the Advancement of Colored People, National Council of La Raza, RM-8491 (Public Notice, DA 94-777, July 14, 1994).

143 NECTA Motion for Investigation (NECTA Motion).

144 Id. at 4.

action, including issuing a cease and desist order.[145]

41. NECTA contends that there is evidence to support its claims. NECTA asserts that, in a proceeding before the Connecticut Department of Public Utility Control (DPUC), SNET stated that it planned to begin construction of its video dialtone facilities in areas encompassed by its pending expansion request before the Commission acted on the request.[146] NECTA also offers declarations of cable television company personnel who claim that they have observed SNET technicians installing optical fiber and coaxial cable distribution facilities.

42. NECTA argues further that the facilities constructed by SNET prior to receiving Section 214 approval are intended for transmission of video programming. According to NECTA, such facilities constitute a significant portion of the costs related to SNET's video dialtone proposal. NECTA also finds support for its argument in SNET's intention to use its video dialtone network exclusively to transmit video programming in its technical trial.

43. SNET argues that NECTA's motion is another attempt to delay competition in the local video marketplace and that it should be denied.[147] SNET contends that, under Commission precedent, it may deploy facilities prior to Commission authorization if the facilities will be used to provide both interstate and intrastate services.[148] SNET states that the facilities it is deploying are

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145 Id. at 2, 7.

146 Id. at 4, citing SNET Responses to Interrogatories, Request by FiberVision Corporation of Greater Hartford Concerning Activities of C.A.I. Wireless, Inc. and Southern New England Telephone Company, DPUC Docket No. 94-02-18 (March 25, 1994). In response to a FiberVision interrogatory, SNET stated that deployment of facilities for narrowband and broadband services, including video dialtone, would begin March 28, 1994. SNET Response to Interrogatory No. FV-63. SNET also states in response to an interrogatory that it expected a decision on its expanded trial application between June and September, 1994. Id., citing SNET Response to Interrogatory No. FV-65, DPUC Docket No. 94-02-18.

147 Opposition of The Southern New England Telephone Company to Motion for Investigation at 1 (filed May 23, 1994) (SNET Opposition).

148 SNET Opposition at 2, citing Northwestern Tel. Sys., Inc., 5 FCC Rcd 876, 877 (Com. Car. Bur. 1990).

part of its network modernization program called "I-SNET".[149] According to SNET, the I-SNET network will offer both narrowband and broadband services, including local exchange service.[150] SNET states that the I-SNET modernization program is not driven by the desire to provide video dialtone, and would exist even in the absence of the video dialtone trial and video dialtone itself.[151] SNET notes that the DPUC is overseeing its modernization program, and that, while the DPUC does not pre-approve SNET's construction, it "support[s] and encourage[s] [SNET's] modernization and development efforts."[152]

44. SNET states that it is currently limiting its construction to facilities to be used for both local exchange and video dialtone services.[153] Specifically, SNET says that it is "constructing the transport component of I-SNET," such as interoffice fiber optic cable and coaxial cable.[154] SNET indicates that it has not deployed any equipment other than fiber optic and coaxial cable, supporting strand and fiber distribution bays.[155] Finally, SNET maintains that it will deploy no video dialtone specific facilities or equipment until it obtains Section 214 authorization.[156]

Discussion

45. The issue presented by the NECTA motion is whether SNET's construction of facilities as part of its I-SNET network upgrade

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149 SNET Opposition at 4.

150 Id.

151 See Request by FiberVision Corporation of Greater Hartford Concerning Activities of C.A.I. Wireless, Inc. and Southern New England Telephone Company, DPUC Docket No. 94-02-18, Decision (July 27, 1994) (DPUC Decision) at 6, attached to SNET Ex Parte letter (Aug. 4, 1994).

152 Letter from Eugene J. Baldrate, Director-Federal Regulatory, SNET, to Todd Silbergeld, Attorney, Policy and Program Planning Division, Common Carrier Bureau, FCC, dated May 27, 1994 (Baldrate Letter).

153 SNET Opposition at 2; see Affidavit of Fred T. Page (Page Affidavit) at paras. 4, 5.

154 Page Affidavit at para. 4.

155 See SNET Ex Parte Letter (Aug. 19, 1994), Attachment.

156 SNET Opposition at 2; Page Affidavit at para. 5.

before receiving Section 214 certification constitutes a violation of Section 214 of the Act. NECTA has not persuaded us that SNET has violated Section 214, or that any further investigation of this issue is warranted. We conclude that the network upgrades and modernization efforts that SNET has undertaken to provide local exchange service do not require Section 214 certification.

46. Section 214(a) of the Communications Act, as amended, prohibits a carrier from constructing a "new line" or an extension of a "new line," or from engaging in transmission over or by means of such a line, "unless and until there shall first have been obtained from the Commission" a certificate of public convenience and necessity. The Act defines "line" as "a channel of communication established by use of appropriate equipment, other than a channel of communication established by the interconnection of two or more existing channels."[157] Section 214 specifically exempts from the certification requirement "a line within a single State unless such line constitutes part of an interstate line."[158]

47. In New Jersey Bell, the Commission found that facilities consisting of telephone-only and dual-use equipment installed by New Jersey Bell (NJB) prior to receiving Section 214 certification were intrastate in nature, and that the installation did not constitute premature construction.[159] The Commission also found that the construction constituted part of a network upgrade planned by New Jersey Bell and approved by its state regulator for the provision of local exchange service and independent of whether the facilities would be used for video dialtone.[160] Because New Jersey Bell started the construction pursuant to the planned network upgrade, and because the installed facilities would primarily be used to provide local exchange, but not video dialtone, service, the Commission determined that the construction NJB started before obtaining Section 214 certification did not constitute the construction of an interstate line of communication.[161] The Commission stated, however, that Section 214 certification was necessary before New Jersey Bell installed video-only equipment or video-specific components of dual-use facilities.[162]

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157 47 U.S.C. § 214(a).

158 Id.

159 New Jersey Bell Tel. Co., FCC 94-180 (released July 18, 1994) at para. 59.

160 Id. at para. 64.

161 Id. at paras. 59, 64.

162 Id. at para. 62.

48. The instant motion involves virtually the same set of facts. As in New Jersey Bell, there are three types of facilities at issue: facilities to be used solely for the provision of telephone service; facilities to be used for both telephony and video dialtone service; and facilities to be used solely for the provision of video dialtone. SNET states that it has begun construction of the second type of facility as part of its I-SNET network modernization, but not the third -- those facilities used only for video dialtone.[163] SNET states that facilities useful only to provide video dialtone service will not be deployed until it receives Section 214 certification from the Commission. Indeed, SNET indicates that it will await Section 214 approval before deploying any equipment other than fiber optic and coaxial cable, supporting strand and fiber distribution bays.[164] No party has contradicted SNET's argument that it has not deployed any video-only facilities. Therefore, the record indicates that the facilities that SNET has constructed to date are all needed for the provision of local exchange service.

49. Under these circumstances, we conclude that the facilities constructed to date will be intrastate in nature. NECTA argues that SNET's proposal to provide a video dialtone trial over its upgraded network before providing local exchange telephone service is evidence that the facilities SNET is constructing are for the video dialtone services proposed in its application. The record shows, however, that SNET intended to upgrade its network for local exchange service independent of its proposal to provide video dialtone service,[165] and that the DPUC has endorsed, and will oversee, this upgrade.[166] The fact that SNET will conduct a video dialtone trial over its upgraded network before using the network for local exchange service does not change the purpose of its construction and, hence, the regulatory requirements associated with that construction. In addition, the record indicates that the facilities SNET is constructing are required for the provision of local exchange service and will be used for video dialtone services only if authorized by the Commission.[167]

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163 SNET Opposition at 2-3; Page Affidavit.

164 See SNET Ex Parte Letter (Aug. 19, 1994), Attachment at 1.

165 See DPUC Decision at 6.

166 See, e.g., Application of the Southern New England Telephone Company to Amend its Rates and Rate Structure, DPUC Docket No. 92-09-19, Decision (July 7, 1993) at 33, attached to Baldrate Letter.

167 SNET Opposition at 2, 3 n.4; SNET Ex Parte Letter at 1 (June 10, 1994).

50. We therefore conclude that no Section 214 certification is required prior to the deployment of the facilities in question because the record shows that the facilities that SNET has constructed to date are needed for local exchange service, and would be deployed even in the absence of video dialtone. Moreover, our interpretation of the application of Section 214 to SNET does not place interstate ratepayers at risk. The Commission stated in the VDT Order that it would use the Section 214 process to apply its antidiscrimination and cost allocation safeguards to specific video dialtone proposals, and we have done so here.[168] At the time telephony is offered over the I-SNET and video dialtone network, SNET states, it will comply with the Commission's then-existing cost allocation rules.[169] In fact, we are conditioning grant of SNET's application on Commission approval of an accounting and cost allocation plan consistent with Commission rules before SNET offers local exchange and exchange access telephone services over the upgraded network during the trial.[170] SNET's construction of part of its broadband network pursuant to a plan endorsed by the Connecticut DPUC before obtaining a Section 214 certification will not eliminate the Commission's ability to apply these and other safeguards.[171] Moreover, no costs related specifically to video dialtone can be allocated to the interstate jurisdiction until the Commission grants Section 214 certification.

E. Motion to Reopen the Record

Contentions of the Parties

51. On October 21, 1994, FiberVision submitted a motion to reopen the record in the proceeding, arguing: (1) that SNET has underestimated the penetration rate for the expanded trial to justify the large trial size, and (2) that SNET has offered unauthorized video dialtone service during its West Hartford trial.[172] FiberVision also argues that the expanded trial is unnecessary because, based on statements by a SNET official, its West Hartford video dialtone pilot has been successful in achieving

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168 See supra paras. 23-30.

169 Id.

170 See supra para. 29.

171 See DPUC Review of Telecommunications Policies: Infrastructure Modernization, Competition, Pricing Principles and Methods of Regulation, Decision, Docket No. 91-10-06 (July 7, 1993).

172 FiberVision Motion to Reopen the Record (FiberVision Motion) at 1-2.

significant consumer response.[173] FiberVision contends that, even if the public interest supports a second, larger trial, the number of homes to be passed by SNET should be significantly reduced because SNET has achieved a penetration rate of 40 percent in its West Hartford video dialtone pilot.[174] FiberVision requests that the Commission compel SNET to release the results of a market survey commissioned by SNET, and completed by the Saugatuck Marketing Group, that may show that SNET's proposed penetration rate for the expanded trial has been underestimated.[175]

52. FiberVision also alleges that SNET has exceeded the authority granted in the SNET Trial Order by offering video dialtone service in West Hartford for at least four months before informing the Commission that the trial had commenced. According to FiberVision, SNET misreads the SNET Trial Order as allowing it to offer video dialtone service for an unspecified period, and then eventually declare the official trial start date "for regulatory purposes."[176] FiberVision claims that, as a result of this erroneous interpretation, SNET will have the ability to offer video dialtone service for 19 months based on an authorization that only permits a trial of 12 months.[177]

53. SNET asserts that the record in this proceeding is complete and that FiberVision's motion is without merit.[178] SNET clarifies that the 12 to 13 percent penetration estimate for the expanded trial is based upon homes passed, while the 40 percent figure cited by FiberVision is based upon video dialtone penetration of homes with cable television in West Hartford.[179] SNET states that, as of September 30, 1994, the penetration rate for the West Hartford pilot was 29 percent.[180] SNET argues that the

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173 FiberVision Motion at 3.

174 Id., quoting Warren's Cable Regulation Monitor, Oct. 17, 1994, at 1.

175 FiberVision Reply at 3.

176 FiberVision Reply at 4, citing SNET Opposition to Motion to Reopen the Record at 3.

177 FiberVision Reply at 4.

178 SNET Opposition to Motion to Reopen the Record at 1.

179 Id. at 2.

180 Id. SNET indicates that the system currently passes 1,250 homes. Id. Under the terms of the West Hartford pilot authorization, SNET is permitted to pass no more than 1,600

penetration estimate for the expanded trial is reasonable, even in light of the current 29 percent penetration rate for the West Hartford test, because, in contrast to the West Hartford test, SNET will impose charges for transport over the video dialtone system during the trial on video programmer-customers who, in turn, will most likely charge end user-subscribers.[181] SNET states that it anticipated a greater penetration rate in the West Hartford pilot because of its small size, which has enabled SNET to conduct intensive marketing and customer service efforts.[182]

54. In response to FiberVision's allegation that SNET provided unauthorized video dialtone service during its West Hartford trial, SNET contends that the Commission granted it permission to begin its trial in West Hartford within one year of the date of the authorization, and that, consistent with the order, the "roll-out" of trial service began after the authorization was granted.[183] According to SNET, the roll-out process continued gradually, "ultimately achieving a sufficient number of end users and Programmer-Customers to 'officially' commence the trial for regulatory purposes on July 1, 1994."[184]

Discussion

55. We reject FiberVision's argument that we should require SNET to reduce the size of the expanded trial because SNET has achieved a penetration rate of 29 percent in its West Hartford test.[185] We find the West Hartford test and the proposed expanded trial to be different undertakings. Based on this record, we believe that the 13 percent penetration estimate for the expanded

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homes.

181 SNET Ex Parte Letter (Nov. 1, 1994) at 2.

182 According to SNET, the West Hartford trial's small size has enabled it to telemarket, canvass door-to-door, use direct mail, and conduct small focus groups and service demonstrations. SNET Opposition to Motion to Reopen the Record at 2; SNET Ex Parte Letter (Nov. 1, 1994) at 2. All of these activities, SNET claims, have significantly contributed to the 29 penetration rate attained in the West Hartford trial. SNET Opposition to Motion to Reopen the Record at 2.

183 SNET Opposition to Motion to Reopen the Record at 3.

184 Id.

185 SNET has clarified that it has achieved a penetration rate of 29 percent in the West Hartford trial area. See supra para. 53 and note 179.

trial is not an unreasonable estimate, even in light of the West Hartford test's 29 percent "take rate," because: (1) SNET is not charging programmer-customers or end users for video dialtone service in the West Hartford technical trial; (2) the size of the West Hartford test is substantially smaller than the proposed expanded trial; and (3) SNET has been able to engage in intensive marketing and promotional activities because of the size of the West Hartford trial. FiberVision contends that the possible use of mass media marketing for the expanded trial weakens SNET's argument that a 13 percent penetration rate is reasonable. We believe that a 13 percent penetration rate estimate is not an unreasonable estimate, even given the possible use of mass advertising campaigns. Sustained service during the trial to a significant proportion of homes passed will depend on many factors, including price, quality of video service, and overall customer service.

56. We also conclude that SNET has not exceeded the authority granted by the Commission in the SNET Trial Order. The record indicates that SNET commenced construction and operation of its West Hartford video dialtone pilot after receiving Section 214 certification from the Commission. Thus, there is no reason based on the record before us to deny SNET permission to expand its video dialtone trial. We find, however, that SNET's West Hartford trial began, for purposes of the 12-month trial authorization, on April 1, 1994, and not on July 1, 1994 as SNET has stated to the Commission.[186] On or about September 28, 1994, Ronald Serrano, Senior Vice President-Corporate Development for SNET, stated that SNET's market share of homes with cable television in the West Hartford trial area was "above 40 percent" and "service has only been available for six months."[187] Although the Commission gave SNET significant latitude in determining the official start date for its trial in West Hartford, we believe that the official start date of this trial should not be significantly later than what is implied by a public statement regarding the trial's performance by a senior officer of SNET. We therefore find that the West Hartford trial's official start date was April 1, 1994. Based on our determination here that the West Hartford video dialtone trial started April 1, 1994, we will require SNET to file the 6-month report mandated in the SNET Trial Order within 30 days of the release of this order.[188] Finally, we reject FiberVision's request that we compel SNET to release the results of the Saugatuck market study because we

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186 See Letter of Eugene J. Baldrate, SNET to Acting Chief, Common Carrier Bureau (June 21, 1994).

187 Speech of Ronald Serrano, Senior Vice President-Corporate Development, SNET at Convergence 1994 Interactive Teleconference Exposition, Sept. 28-30, 1994.

188 SNET Trial Order at 1023, para. 21(e).

believe that the record in this proceeding is complete and enables us to grant SNET's request to expand its video dialtone trial.

IV. ORDERING CLAUSES

57. Accordingly, **IT IS ORDERED**, that, pursuant to Section 214 of the Communications Act of 1934, as amended, 47 U.S.C. § 214, the Request of The Southern New England Telephone Company (File No. W-P-C-6858) **IS GRANTED**, and the applicant is authorized to expand its video dialtone trial by passing no more than 150,000 homes and businesses in certain towns indicated herein in its Stamford and Hartford, Connecticut service areas for a period of one year from the date the first customer is taking service under an effective interstate tariff for the market trial. We instruct SNET to inform the Secretary of the Commission and the Chief, Common Carrier Bureau, of the date the first customer is taking video dialtone service under an effective tariff.

58. **IT IS FURTHER ORDERED**, that grant of the application for the hybrid fiber-coaxial trial proposed herein **IS SUBJECT TO** the following **CONDITIONS**:

a) That SNET inform participants in the expanded trial, including both programmer-customers and video dialtone service subscribers, that SNET is conducting a trial of video dialtone services, that the trial is limited to one year, and that SNET may or may not offer video dialtone on a commercial basis after the conclusion of the trial.

b) That SNET account for all costs associated with the expanded trial, including development costs and expenses, in accordance with Part 32 of our Rules. SNET must also create subsidiary accounting records to capture the revenues, investments, and expenses associated with the provision of its video dialtone service and file accurate copies of those records for public inspection with the Secretary of the Federal Communications Commission on a quarterly basis. Copies of these records must also be served on the Chief, Accounting and Audits Division, Common Carrier Bureau. We delegate to the Chief, Common Carrier Bureau the authority to determine the content and format of the subsidiary accounting records as well as the quarterly reports. In the event SNET wishes to offer local exchange and exchange access telephone service over the upgraded network during the trial, SNET must first submit and obtain approval of an accounting and cost allocation plan. We delegate to the Chief, Common Carrier Bureau the authority to review and approve the accounting and cost allocation plan submitted by SNET.

c) That SNET file any necessary revisions to its Cost Allocation Manual within thirty days after release of this Order, and sixty days before providing non-regulated services

related to video dialtone. SNET must also list all accounts affected by its provision of non-regulated services associated with the video dialtone trial, and describe those services.

d) That SNET not participate in any decisions concerning the selection, packaging, pricing, bundling, or tiering of video programming to end-users absent prior Commission approval. This authorization does not permit SNET, either directly or indirectly through an affiliate, to provide video programming directly to its subscribers.

e) That SNET provide all video programmers access to the basic platforms under the same terms and conditions and undertake all reasonable steps to expand capacity as necessary to meet demand.

f) That SNET notify the Chief, Common Carrier Bureau (with copies to the Chiefs of the Policy and Program Planning Division and the Domestic Facilities Division) within thirty (30) days of becoming aware of a capacity shortfall, or within five (5) days after denying a video programmer access to the video dialtone platform because of capacity limitations, whichever occurs first. Should SNET conclude that expansion of the platform's capacity for the trial is not technically feasible or economically reasonable, it must, at that time, explain in detail the basis for its determination.

g) That SNET comply prospectively with any changes in our rules that result from rulemakings or from reconsideration of the VDT Order in CC Docket No. 87-266.

h) That SNET submit to the Chief, Common Carrier Bureau, six months after commencement of the expanded trial and within sixty (60) days of the end of the expanded trial, a written report. The report must, among other things:

1) include a statement from each video programmer or other service provider using SNET's services stating whether that programmer/service provider believes it has been discriminated against by SNET in any manner;

2) identify the capacity allocated to each video programmer customer and the identity of the programmer-customer;

3) describe the video dialtone technology used during the trial. SNET must include information on the video switch and other components of the video dialtone system, the operation of video-on-demand, the quality of the video, the methods of accessing the platform, and the digital technology incorporated into the network and its impact on capacity;

4) to the extent known, evaluate the market for video dialtone service, providing penetration rates on a monthly basis, and describing consumer interest in on-demand video services and consumer willingness to pay for video dialtone service;

5) detail the costs, both direct and common, SNET has allocated to the trial broken down into subsidiary accounting records; and,

6) include any published commentary of which SNET is aware regarding the trial.

59. **IT IS FURTHER ORDERED**, because we have determined that the official start date of the West Hartford trial was April 1, 1994, that SNET is required to file the 6-month West Hartford trial report within 30 days of the release of this order.

60. **IT IS FURTHER ORDERED** that the Motion for Investigation filed by the New England Cable Television Association on March 13, 1994 **IS DENIED** for the reasons stated herein.

61. **IT IS FURTHER ORDERED** that the Motion to Reopen the Record filed by the FiberVision Corporation on October 21, 1994 **IS DENIED** for the reasons stated herein.

62. **IT IS FURTHER ORDERED** that pursuant to Section 214(c) of the Communications Act of 1934, as amended, 47 U.S.C. § 214(c), the grant of SNET's application to provide video dialtone service is subject from the date of release of this grant to the conditions contained herein, and is also subject to any Commission rules or orders that result from any existing or future proceeding or proceedings that address video dialtone cost allocations, jurisdictional separations, and pricing issues. Failure of The Southern New England Telephone Company to decline the authorization as conditioned within thirty-one (31) days from the release date will be construed as formal acceptance.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

SEPARATE STATEMENT

OF

COMMISSIONER ANDREW C. BARRETT

RE: The Southern New England Telephone Company, Video Dialtone 214 Authorization

This Order and Authorization grants the request of Southern New England Telephone Co. (SNET) to extend and amend its existing Section 214 authorization to conduct a technical and market trial of video dialtone services in several towns in Connecticut for a period of one year. In particular, SNET proposes to expand its market trial by passing 75,000 homes in each of two geographic areas, for a total of 150,000 homes.[1] SNET has claimed that a trial of this size, which SNET claims will be based on a penetration of 12-13 percent, or approximately 20,000 homes for the two combined areas, will enable SNET to obtain statistically valid data on a variety of variables -- such as employment, income, lifestyle, geography, behavior, and a comparison of the two areas -- over a relatively brief time horizon as compared to other trials. Accordingly, this Order finds that: (1) SNET's proposal meets the video dialtone requirements of offering a basic common carrier platform with sufficient capacity to serve multiple video programmers; and (2) SNET will be required to demonstrate that its video dialtone rates will recover all direct costs of the market trial and a reasonable allocation of overhead costs.

In this proceeding, opponents have questioned SNET's request to expand the market trial because of the proposal to pass an unprecedented number of homes, with particular scrutiny of SNET's estimated penetration rate for the expanded trial. I support the Commission's determination that, based on the proceeding's record, SNET's estimated penetration level for the expanded trial is not unreasonable. In this regard, the Order provides for reporting requirements and cost allocation safeguards to ensure that the interests of telephone ratepayers, video dialtone subscribers, and programmer customers are protected. I write separately, however, to emphasize my concern that the unusually large number of homes passed during this trial may continue to raise consumer and competition implications that the Commission will need to monitor, especially given the uncertainty regarding the actual penetration that will be realized during the expanded trial. As a result, I will be interested to review the results of SNET's expanded test of video dialtone services as they are reported to the Commission.

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[1] SNET has proposed to serve northern Connecticut towns of West Hartford (excluding the previously approved area), New Britain, Farmington, and Hartford. In the second area, SNET seeks to serve Stamford, Norwalk, Darien, Westport, and Fairfield.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

DA 94-526

In the Matter of	)
	)
Cable Operators' Rate Justification	)
Filings, Sections 76.945, 76.956	)
of the Commission's Rules	)

ORDER

Adopted: May 20, 1994 Released: May 23, 1994

By the Acting Chief, Cable Services Bureau:

1. Under the Cable Television Consumer Protection and Competition Act of 1992, cable operators have the burden of proving that the rates they seek to charge for regulated services are lawful. Cable Services Bureau review of cable operators' rate filings, both benchmark filings on FCC Form 393 and cost-of-service filings, reveals certain problems. Operators have in some cases failed to provide adequate information to allow meaningful analysis of the reasonableness of the rates. In other cases, operators have failed to use the required form. We set forth here certain guidelines with respect to both pending and future cable rate filings with the Commission, and we establish a period, until June 24, 1994, during which cable operators may incorporate these corrections and resubmit rate support filings.[1]

Benchmark Filings

2. Presently pending before the Commission are several thousand filings on FCC Form 393 submitted by cable operators seeking to justify their cable programming service rates.[2] In its *Third Reconsideration* the Commission recently

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[1] Absent action by the local franchising authority, this Order does not alter any existing obligations of cable operators with regard to provision of data to local franchising authorities.

[2] See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation, MM Docket 92-266, Report and Order and Further Notice of Proposed Rulemaking, FCC 93-177, 8 FCC Rcd 5631 (1993) (Rate Order) at paras. 214-215 and Attachment D. FCC Form 393 is "Determination of Maximum Initial Permitted Rates for Regulated Cable Programming Services and Equipment." Cable operators file this form with local franchising authorities in response to notification that the local franchising authority is certified and is regulating basic service tier rates, and also with this Commission in response to a complaint on FCC Form 329 about rates charged for the cable programming service tiers.

noted that many of these filings appear not to comply with our rules, and required operators to replace these defective filings by May 29, 1994.[3]

3. The Cable Services Bureau has reviewed the original Form 393 filings in greater detail, and has identified a number of common deficiencies in addition to those identified in the Third Reconsideration. We are therefore creating an expanded window of opportunity for operators to correct their filings, and are listing here the more significant problems noted to date and indicating what is required:

(1) **Rate justification required, but not filed.** The cable rate regulation rules require the filing of a Form 393 rate justification whenever the Commission receives a Form 329 complaint regarding cable programming service rates that it does not return to the complainant within 30 days. The filing is required even if the operator requests dismissal of the complaint, and even if the operator chooses to file a cost-of-service showing.[4]

(2) **Unofficial form used.** Many operators filed their justifications on unofficial substitute forms that are not "identical in overall appearance and format" to the official Form 393, as required in the November 10 Public Notice.[5] Because of the burden entailed in processing a variety of such substitute forms, the Commission in the *Third Reconsideration* required that all filers who used substitute forms transfer their data to an official Form 393 and refile.[6]

(3) **Justification not based on single franchise area.** Form 393 filings must justify the rates charged in a single franchise area, as denoted by a single community unit identification (CUID) code. Data reflected on Form 393 must relate to

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[3] The Commission ordered that operators that had filed on noncomplying forms must refile on official FCC forms within 14 days after the effective date of the Order. The Commission also stated that many filings were apparently defective or incomplete, and reiterated the authority of the Commission to require supplementation of such filings. The Commission noted that many basic service rate justifications filed with franchising authorities were also defective, and reminded authorities of their discretion to require amended filings. See Implementation of Sections of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation, MM Docket Nos. 92-266 and 92-262, Third Order on Reconsideration, FCC 94-40 (released March 30, 1994), 59 Fed. Reg. 17961 (Apr. 15, 1994) (Third Reconsideration) at paras. 98, 86-92.

[4] See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215, FCC 94-39, released March 30, 1994, 59 Fed. Reg. 17975 (Apr. 15, 1994) (Cost of Service Order) at para. 36, n.58.

[5] Public Notice, released Nov. 10, 1993.

[6] Cost of Service Order at para. 98. The Cable Services Bureau recently ruled that operators may also file a substitute Form 393 prepared using a spreadsheet program written by Economists Inc. See FCC Form 393: Economists, Inc., Order, DA 94-465 (released May 6, 1994).

that specific franchise area except where specifically allowed otherwise. However, some operators have apparently filed reports for, or submitted data encompassing, (for example) an entire system, thus improperly including more than one franchise area.

(4) **Complaints not attached.** Operators filing Form 393 with the Commission must attach a copy of the Form 329 complaint(s) they are responding to.

(5) **Additional attachments.** In the *Third Reconsideration* the Commission required that rate justifications filed on or after May 15, 1994, include copies of rate cards for the rates in effect as of September 30, 1992, and September 30, 1993, as well as for the rates being justified.[7] While justifications filed previously are not defective without rate cards, filings on or after May 15, 1994, including refilings, will be deemed nonconforming if filed without rate cards. (In addition, we encourage operators to specify clearly: (a) the operator's organizational form -- sole proprietorship, partnership, Subchapter S corporation, C corporation or other -- to permit verification of proper tax treatment; and (b) the number of regulated channels and the number of regulated satellite channels on their systems, to permit verification of benchmark rate determinations.)

(6) **Basic rates portions of Form 393 left blank.** Some operators have left blank portions of Form 393 summarizing the permitted and actual rates for basic cable service and related installation and rentals. Operators must submit a fully completed Form 393.

(7) **Required descriptions and explanations omitted or inadequate.** Perhaps the most common deficiency is that many operators have overlooked the requirement at several places in Form 393 (especially in Part III) to attach explanations for, or identify, the entries on their forms. Others have submitted only general statements that do not explain their entries, and do little more than affirm compliance with the form's instructions. More is required. Explanations must be provided where required, and must show the specific calculations used to reach the result entered on the form, as well as clearly identifying the nature and source of the data employed. Where the original data is estimated (for example, time estimates and percentage allocations), the basis of the approximation must be explained in sufficient detail to demonstrate its reasonableness. Types of equipment (such as converters or remote controls) must be clearly described, preferably by manufacturer and model number.

(8) **Incorrect price indexes used.** Some operators have overlooked the Commission's November 10, 1993, public notice clarifying that filings must reflect the most recent price index information published by the U.S. Department of

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[7] Third Reconsideration at para. 92.

Commerce, and instead have used a preliminary figure for the third quarter of 1992, as printed on Form 393. Calculations involving Part II of Form 393, Worksheet 1, Line 123, should use the corrected figure 122.5. For the convenience of all who must complete or review Form 393's, the following table lists the most recent price index figures:

3rd Quarter 1992	122.5
4th Quarter 1992	123.4
1st Quarter 1993	124.7
2nd Quarter 1993	125.6
3rd Quarter 1993	126.2
4th Quarter 1993	126.9

(9) **Other mathematical errors**. We have noted frequent calculation errors, which could be minimized by rechecking all calculations, or by using the Commission's spreadsheet program for generating Form 393.[8]

(10) **Rate justifications not corrected as required**. The Commission's rules hold filers responsible for the continuing accuracy and completeness of information furnished to the Commission. See 47 C.F.R. § 1.65. However, some operators have apparently updated the Form 393's filed with franchising authorities, without amending their filings with the Commission.

4. Unless these and other deficiencies are promptly corrected, they may prevent the Commission from finding that an operator has met its burden of justifying its rates. In such circumstances the Commission may prescribe rates for cable programming service, and order refunds for past overcharges.

5. To avoid both this result and the associated administrative inefficiencies, and in order to provide ample opportunity for operators to furnish complete and accurate rate justifications, we hereby establish a window of opportunity, until June 24, 1994, for operators to review, correct, and resubmit their filings in light of the guidance in this Public Notice.[9]

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[8] This spreadsheet is being released concurrent with this Order; see Public Notice of May 23, 1994.

[9] This Public Notice permits operators to supplement and correct their 393 filings. Some operators are also subject to the Commission's refling requirement, announced in the Third Reconsideration, pertaining to use of authorized forms. Rather than filing twice within one 30-day period to effect compliance with Commission and Bureau requirements, operators may submit a single filing on June 24, 1994, incorporating the changes described here as well as that required by the Commission. Such a submission should be accompanied by a Motion to Accept Late-filed Submission. Operators whose resubmissions address only the Commission's authorized forms requirement must meet the May 29 deadline.

6. This resubmission opportunity does not relieve operators from possible penalties for violation of our rules in connection with their initial rate filings (or lack thereof). In order to preserve the integrity of our cable rate regulation process, we will impose forfeitures and other sanctions as appropriate, to the extent permitted under our rules. We note also, however, that the Commission has stated that operators will not be penalized for making good faith attempts to comply with our rules in a timely manner.[10]

Cost-of-Service Filings

7. Following preliminary review of pending cost-of-service filings from cable operators, Cable Services Bureau staff notes that some of these filings appear to lack significant data. The Bureau is accordingly allowing the same window noted above for refiling of FCC Form 393, for cable operators to modify or supplement their cost-of-service (COS) filings in light of the staff observations and comments noted below.

(1) **Incomplete filings.** Some filings are missing relevant material. For example, each COS filing should attach the complaint(s) to which it is responding, and the rate card that was current at the time of the complaint. Every COS filing should also include a benchmark calculation (on Form 393), since COS is an alternative ratemaking methodology to be used when the operator believes the benchmark rate is inadequate. Many of the pending filings do not include these attachments; they should be modified to correct this omission.

(2) **More detail needed.** In other cases, required information is provided in some form, but additional detail is needed. For example, while general cost-of-service principles allow for inclusion of some intangible costs in the ratebase, they do not allow for inclusion of all intangibles. A COS showing that lists 'intangibles' without further elucidation or support does not provide a level of justification or detail that would allow us to approve inclusion of any intangibles, despite our awareness that some part of the operator's intangibles might well be allowable. Similarly, a showing that includes 'goodwill and customer lists' does not allow us to determine what part, if any, of such costs might be allowable, since general cost-of-service principles normally exclude goodwill, but may allow some customer list costs.

8. A showing that fails to provide detail adequate to permit us to determine what, if any, part of costs should be allowed may result in the disallowance of all such costs.

(3) **Need explanation of methodology used.** Some of the pending COS filings discuss various valuation and justification methodologies without making

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[10] Third Reconsideration at para. 93.

clear what approach they are using. For example, some operators discuss valuation methodologies for plant in service to be included in the ratebase, then list a plant amount without explaining what methodology produced this number. Filings should always make clear how their amounts were derived. In our example, since original cost is the acknowledged "general cost-of-service principle" valuation methodology, operators should note the plant value this methodology produces (or an estimate, noting how the operator calculated it), as well as the value the operator is seeking to justify and the valuation methodology used to produce this value.

9. Filings that fail to clarify how numbers shown were calculated are incomplete and may leave the cable operator in default. In this situation, the Bureau will develop rates upon the best available information, using general cost-of-service principles. This could result in a substantial impact on the operator's rates.

(4) **General cost-of-service principles.** The COS filings before us were submitted prior to the effective date of the Commission's rules that were set forth in the March 30 Cost of Service Order, and are thus based on "general cost-of-service principles."[11] While COS filings submitted prior to the effective date of the rules will not be held to the new rules, operators might well review the COS forms established by the Cost of Service Order (FCC Forms 1220 and 1225) to understand the level of detail we seek, and the degree of justification we consider essential to the support of rates above the benchmark rate. Review of the forms will also reveal the points on which we rely in our evaluation of rates, thus providing guidance to operators in ascertaining where their filings might benefit from supplementation.

10. Rates supported by cost-of-service showings will be set at the level the showing supports; a COS showing that is incomplete or lacking may result in our setting the rates at a lower level, if costs are not justified and are thus disallowed.

11. Operators having COS filings currently pending may take the opportunity, during this window, to reevaluate their COS showings and, if they choose, to withdraw the pending COS filing and rely on the benchmark rate established in their Form 393 filing. Operators electing this approach should so notify the Bureau by letter, no later than June 24, 1994. Operators electing to supplement or refile their COS submissions should do so by June 24, 1994.

Ordering Clauses

12. Accordingly, IT IS ORDERED, pursuant to Section 4(i) of the Communications Act of 1934, as amended, 47 U.S.C. 154(i), and Sections 623(c),

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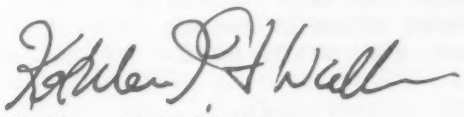
[11] These filings are submitted under Section 76.956(b)(2)(ii) of the Commission's rules, 47 C.F.R. §76.956(b)(2)(ii), which requires a "detailed cost showing" based on general cost-of-service principles.

0.291, and 0.321 of the Commission's rules, 47 C.F.R. §§ 543(c), 0.291, and 0.321, that those cable operators wishing to supplement their rate support filings as discussed above SHALL REFILE no later than June 24, 1994.

13. IT IS FURTHER ORDERED that to the extent that such filings incorporate the forms uniformity changes required by the Commission, and these changes have not previously been filed, the June 24, 1994 filing SHALL BE FILED WITH a Motion to Accept Late-filed Submission.

FEDERAL COMMUNICATIONS COMMISSION



Kathleen M. H. Wallman
Acting Chief, Cable Services Bureau

FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

IN REPLY REFER TO:

DA 94-521

May 20, 1994
Released: May 23,1994

The Disney Channel c/o
Mr. Frederick Kuperberg, Esq.
Senior Vice-President
Business and Legal Affairs
3800 West Alameda Avenue
Burbank, CA 91505-6070

Dear Mr. Kuperberg:

This letter is in response to your May 6, 1994 inquiry seeking clarification of two letters we released April 14, 1994 and April 19, 1994 concerning the impact of Section 76.922(b)(6)(B) on the addition or substitution of a new programming service to a regulated cable service tier prior to July 14, 1994.[1] You state that, since before April 1993, The Disney Channel has been discussing with cable operators currently carrying The Disney Channel as an unregulated per-channel offering the possibility of relocating carriage of the service to cable programming service tiers potentially subject to regulation. You state that the parties waited to finalize the relevant affiliation agreement amendment until the Commission released its revised rate regulations on March 30, 1994, but now require further clarifications before going forward.

First, you note that we stated in the Second fX Letter that, under the conditions described there, an operator's addition or substitution of a new programming service in a regulated tier during the deferral period, without any increase in rates and pursuant to the previous plans of the operator, will not constitute a service and rate restructuring that would trigger refund liability under Section 76.922(b)(6)(B) of the Commission's rules.[2] You seek clarification of whether this

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[1] See In re fX Channel (released April 20, 1994, Cable Services Bureau) and In re fX Channel (released April 22, 1994, Cable Services Bureau) (clarifying impact of 47 C.F.R. § 76.922 on the June 1, 1994 launch of fX).

[2] In the context of channel substitutions, we limited this finding to situations in which the cost of the new channel is at least as high as the cost of the one replaced. In re fX Channel

finding may also apply to program services which, like The Disney Channel, have been carried on an unregulated, per-channel basis by cable systems pursuant to pre-existing contractual affiliation agreements since at least March 30, 1993, and which subsequently agree to be relocated to cable programming service tiers subject to regulation. You state that extending this rule to The Disney Channel will speed delivery of the program service to consumers.

We believe that the circumstances described in your letter are similar to those that formed the basis of our decision in the fX Letters. We understand that you had expended considerable resources, and negotiations were substantially completed by March 30, 1994. Accordingly, we determine that the addition of The Disney Channel to a regulated tier during the deferral period will not trigger refund liability under Section 76.922 of our rules. We limit this determination to the circumstances described in your letter, and additionally to the conditions set forth in the fX Letters.

Second, you note that we stated in the Second FX Letter that operators, under the conditions described there, may include in permitted rates the costs incurred from carriage of new services prior to July 1, 1994. You seek clarification of whether cable operators adding The Disney Channel to regulated cable service tiers and implementing the appropriate rate changes and restructuring between July 1 and July 14, 1994 may immediately include in rates the resulting external programming costs incurred between July 1, 1994 and July 14, 1994.

Under Section 76.922(d)(3)(iii) of the Commission's new rules, "[r]ate adjustments made to reflect changes in external costs shall be based on any changes in those external costs that occurred from the end of the last quarter for which an adjustment was previously made through the end of the quarter that has most recently closed preceding the filing of the FCC Form 1210." Thus, the charges you describe would not be permitted under our rules to be passed through to subscribers between July 1 and July 14, 1994.

We believe, however, that extending our previous waiver of this rule is appropriate in this case because of the transitional issues it raises. We are persuaded that, in fairness to programming services such as The Disney Channel whose negotiations for agreements governing the carriage of new program services were substantially complete prior to release of our revised rate regulations, and in fact, likely would have been finalized but for the uncertainty surrounding when our rules would be released and what forms our going-forward and revised benchmark regulations would take, operators should be permitted

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(released April 22, 1994, Cable Services Bureau), at 1.

to recover in permitted rates the programming costs of such new services incurred between July 1 and July 14, 1994. Where the operator is subject to regulation at the local level, it may include the accrued costs when it makes its first Form 1210 filing.[3] We limit this determination to the introduction of program services during the period for deferral of refund liability, or prior to July 14, 1994. We further limit this finding to the addition of new program services under the circumstances described in your letter. We believe that this approach will facilitate the introduction of program services to consumers by maintaining incentives for operators to introduce new program services in regulated service tiers during the deferral period.

Very truly yours,

Kathleen M.H. Wallman
Acting Chief
Cable Services Bureau

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[3] As stated in the Second FX Letter, we will provide guidance as to how operators should supplement their first Form 1210 filing to ensure that they are able to recover these programming costs.

FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

IN REPLY REFER TO:

DA 94-520

May 19, 1994

Released: May 23,1994

The Disney Channel c/o
Mr. Frederick Kuperberg, Esq.
Senior Vice-President
Business and Legal Affairs
3800 West Alameda Avenue
Burbank, CA 91505-6070

Dear Mr. Kuperberg:

This letter is in response to your April 26, 1994 inquiry seeking clarification of Section 76.922(d)(3)(X) of the Commission's rules as applied to carriage by cable operators of the Disney Channel on regulated cable service tiers. That Section of the rules, and related instructions to FCC Forms 1200 and 1210,[1] require that payments from programmers to cable operators, including rebates, refunds, or other cash incentives, be offset against programming costs for purposes of determining programming costs eligible for external cost treatment.

You state that promotional efforts undertaken by cable operators are the most efficient means for the Disney Channel to market its product to consumers. You note that programmers often purchase advertising time from operators to promote the programmer's offerings. In addition, programmers may reimburse operators for all or part of their marketing expenses related to promoting the program service, including printing and postage costs, ad agency fees, and sales force commissions. You state that these advertising and marketing expenses are neither an element of, nor related to, the programming fee charged to the operator; rather, these costs represent ordinary costs of doing business for the programmer that should not be deemed refunds or rebates of the programming fee; paid by operators to programmers. Your letter describes cable operators' reluctance to add program services to regulated tiers if the Commission requires that these types of payments received from programmers must be offset against programming costs accorded external treatment. You state that this result will deny consumers access to new program services, and contradicts the goal of the 1992 Cable Act to expand the diversity of programming on cable systems.

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[1] See Instructions to Line B2, FCC Form 1200; Instructions to Line B1a, FCC Form 1210.

Accordingly, you seek clarification that direct and verifiable payments from a programmer to a cable operator for costs incurred in advertising and marketing the programmer's offerings do not invoke Section 76.922(d)(3)(X) of the Commission's rules.

Section 76.922(d)(3)(X) is designed to protect subscribers by assuring that external programming costs paid by subscribers are based on the net costs experienced by the operator and fully reflect any rebates or other compensation received by the operator from the programmer. We do not believe that reimbursements of verifiable, reasonable promotional expenses of the type discussed in your letter raise concerns that require offsetting under Section 76.922(d)(3)(X) of the Commission's rules in all circumstances. Accordingly, subject to the limitations stated below, we clarify that Section 76.922(d)(3)(X) of the Commission's rules and the relevant portions of the instructions to FCC Forms 1200 and 1210 do not require a programmer's payments to an operator for advertising time to promote the programmer's offerings, or payments to reimburse the operator for reasonable, documented expenses of marketing the program service to consumers, be offset against increases in programming costs for purposes of calculating charges accorded external treatment.

This determination is limited to situations where, as in the case with Disney, the programmer has routinely and ordinarily reimbursed the cable operator for promotional expenditures prior to the date of this letter. This determination does not permit, absent special circumstances justifying a waiver, programmers to initiate reimbursement of promotional expenses, or significantly expand reimbursements, without the offsetting contemplated by Section 76.922(d)(3)(X) of the rules. This limitation will safeguard against programmers initiating or significantly expanding promotional reimbursements and recovering the reimbursement in higher programming charges to operators that could, in turn, result in higher charges to subscribers under our going-forward rules. At the same time, this approach will permit operators to continue to receive reimbursements that have been part of their normal business practices without offsetting. We will monitor the impact of this determination closely. In addition, we remind industry and consumers that subscribers may file complaints with the Commission concerning changes in rates for cable programming services within 45 days of such changes, and may contact their local franchising authority concerning changes in rates for basic cable service and associated equipment.

We will interpret the foregoing limitation flexibly. As long as, in individual cases, the reimbursements are part of a reasonable marketing plan and it does not appear that the operator and the programmer have significantly altered reimbursement practices primarily in order to avoid offsetting,

we will not require application of Section 76.922(d)(3)(X). In addition, we will not require offsetting for reimbursements for verifiable and reasonable promotional expenses for new program services added to a regulated tier. This will facilitate the provision of new programming services to subscribers, and, does not raise concerns of alteration of past reimbursement practices that could raise rates for consumers. These limitations will not apply to purchase of advertising time from cable operators. As long as the expenditure for advertising is customary and verifiable, we will not require offsetting even if the programmer is undertaking additional advertising expense.

We also limit this determination to the specific types of payments described in your letter. We also require that programmers employ reasonable procedures to verify reimbursable expenses and advertising services purchased from the operator in a form suitable for review by local franchising authorities and the Commission.

Sincerely,

Kathleen M.H. Wallman
Acting Chief
Cable Services Bureau